REVIEW OF THE RECENT AUDITS OF THE EXPORT ENHANCEMENT PROGRAM, TARGETED EXPORT ASSISTANCE PROGRAM, AND GSM–102/103 GUARANTEED CREDIT PROGRAMS BY THE U.S. DEPARTMENT OF AGRICULTURE'S OFFICE OF INSPECTOR GENERAL

JOINT HEARING

BEFORE THE

SUBCOMMITTEE ON DEPARTMENT OPERATIONS, RESEARCH, AND FOREIGN AGRICULTURE

THE

SUBCOMMITTEE ON TOBACCO AND PEANUTS

AND THE

SUBCOMMITTEE ON WHEAT, SOYBEANS, AND FEED GRAINS

OF THE

COMMITTEE ON AGRICULTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

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THURSDAY, NOVEMBER 16, 1989

HOUSE OF REPRESENTATIVES; SUBCOMMITTEE ON DEPARTMENT OPERATIONS, RESEARCH, AND FOREIGN AGRICULTURE; JOINT WITH SUBCOMMITTEE ON TOBACCO AND PEANUTS; SUBCOMMITTEE ON WHEAT, SOYBEANS AND FEED GRAINS; COMMITTEE ON AGRICULTURE,

Washington, DC.

The subcommittees met, pursuant to notice, at 9:35 a.m., in room 1300, Longworth House Office Building, Hon. George E. Brown, Jr. (chairman of the Subcommittee on Department Operations, Research, and Foreign Agriculture) presiding.

Present from the Subcommittee on Department Operations, Research, and Foreign Agriculture: Representatives Brown, Rose, Panetta, Glickman, Hatcher, Olin, Volkmer, Jontz, Roberts, Grandy, and Walsh.

Present from the Subcommittee on Tobacco and Peanuts: Representatives Rose, Hatcher, English, Tallon, Hopkins, and Grant.

Present from the Subcommittee on Wheat, Soybeans, and Feed Grains: Representatives Glickman, Johnson, English, Volkmer, Penny, Nagle, Jontz, Campbell, Long, Marlenee, Roberts, Smith, Schuette, and Grandy.

Staff present: Joseph Muldoon, assistant counsel; Francie Monaghan, clerk; William A. Stiles, Jr., Heidi Pender, subcommittee counsel, Joan Teague Rose, Greg Frazier, Anne C. Keys, Anita R. Brown, James A. Davis, John J. Aguirre, and Richard Jones.

Mr. ROSE. Ladies and gentlemen, this is a joint hearing with the Subcommittee on Department Operations, Research, and Foreign Agriculture, the Subcommittee on Tobacco and Peanuts, and the Subcommittee on Wheat, Soybeans, and Feed Grains. It is to review the recent audits of the Export Enhancement Program, Targeted Export Assistance Program, and the GSM-102/103 guarantee credit programs by the U.S. Department of Agriculture's Officer of Inspector General.

Chairman Brown has been delayed because of the weather, but we are going to make opening statements and begin the hearing. Chairman Brown will be here shortly.

I call on the ranking minority member of the Subcommittee on Department Operations, Research, and Foreign Agriculture, Mr. Roberts, for his opening statement.

OPENING STATEMENT OF HON. PAT ROBERTS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. ROBERTS. I thank the chairman. I want to commend Chairman Rose, Chairman Brown, Chairman Glickman, and various sundry ranking minority members of the appropriate subcommittees for convening this hearing, today.

I want to emphasize the obvious. The fact that we are holding a hearing jointly with two other subcommittees indicates the interest and concern regarding the integrity of our export programs under the purview of the Department of Agriculture.

In 1985, we exported 915 million bushels of wheat. In 1987, wheat exports rose to 1.6 billion bushels; a dramatic increase. The United States' share of the world market during this time frame expanded from 27 percent to 41 percent. There was a corresponding increase in economic activity, economic revitalization in Kansas, the home of Mr. Glickman and myself.

The USDA's Economic Research Service attributes 25 percent of these gains to the success of the Export Enhancement Program. Obviously, the Export Enhancement Program has been immensely successful in expanding market share and in increasing wheat prices; all-in-all, a winning story, or so we thought.

Now, the success of the Export Enhancement Program and other export programs now is in serious question in regard to management. At issue is the management of the Foreign Agricultural Service, and I would say that careless administration of our export programs may not jeopardize the financial existence of the participating grain trading companies, instead it's the small family farmer who may be forced to compete against what I call "fortress" Europe and their unfair trading practices.

Now, I don't want to focus on the well-publicized mistakes of the past. Rather, we need to focus on the response of the USDA policymakers, and we, the Congress and the USDA, had better put these export programs back on the road to respectability. But, we can't forget that the farm bill we pass out of committee next year must pass the scrutiny of our very critical, sometimes, colleagues on the House floor.

I would hope that we would not make any speeches or any statements here that would simply be ammunition to do away with these vital programs. We can't do that.

As it stands right now, all three export promotion initiatives, the Export Enhancement Program, the Targeted Export Assistance Program, and the GSM-102/103 export credit guarantee programs need repair. That is what we are about. It is oversight responsibility. It is shop mechanic work.

We never intended to permanently entrust the USDA with the responsibility of marketing our farm goods. As we discuss and draft the 1990 farm bill, we ought to give very serious consideration to returning to the producer the responsibility for marketing agricultural commodities. We need to develop and implement policies that

make our producers very competitive across the board and in all of our traditional markets.

Let me just say, Mr. Chairman, I know that many on these subcommittees and the full committee have been very critical in regard to policy errors in regard to these export programs. But, as I indicated, our market share is up, and in the situation of wheat, we must have these programs. We must prepare them.

I thank the Chair, and again I wish to commend Mr. Brown, Mr. Glickman, and Mr. Rose for their leadership in holding these hearings.

Mr. BROWN. Thank you very much, Mr. Roberts. The Chair has a brief opening statement, which he will insert in the record at this point, but I do want to thank all of my colleagues on each of the three subcommittees for joining together in this very important oversight activity. I think it will contribute to the force of whatever recommendations that we emerge with.

[The statement of Mr. Brown follows:]

OPENING STATEMENT OF HON. GEORGE E. BROWN, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Today we have three subcommittees joining in an oversight hearing of the agricultural export promotion programs operated at the USDA. We have joined together because each subcommittee has responsibility for and has been involved in oversight of one or more aspects of these programs and their performance.

The goal of today's hearing is to examine in one place and at one time the results of reviews and audits done by the USDA Inspector General and the General Accounting Office on the GSM 102/103 export loan guarantee program, the Export Enhancement Program (EEP), and the Targeted Export Enhancement Program (TEA). We hope to review the adequacy of the Department's response to the problems revealed by these audits over the last few years, at least in the eyes of the auditors. We will be asking USDA the same questions in a subsequent hearing.

We need to know how these programs, which are so important to the continued competitiveness of American agriculture, are being operated. We need to know if there are corrections which need to be made to their authorizations as we prepare for the 1990 Farm Bill. We need to further examine issues of cost-effectiveness, although that is beyond the scope of today's hearing.

I want to thank my colleagues for joining with us today and will recognize them for any comments that they might have.

Mr. BROWN. I would like to recognize Mr. Rose for any opening statement that he may have.

OPENING STATEMENT OF HON. CHARLES ROSE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NORTH CAROLINA

Mr. ROSE. Thank you, Mr. Brown. Mr. Chairman, on October 6, 1988, the Tobacco and Peanuts Subcommittee held a hearing on fraud in the export credit guarantee programs, GSM-102 and GSM-103, looking specifically at shipments of blended foreign and U.S. tobaccos that were sold under the export program as U.S. farmers' tobacco.

The subcommittee was informed that an audit of the export credit programs was underway, and that Government auditors would ascertain the extent to which foreign commodities were misrepresented to our foreign customers as U.S. agricultural commodities.

This audit started over 2 years after I first notified USDA's FAS, that the subcommittee had received a complaint regarding the

shipment of foreign tobacco under the GSM-102 and GSM-103 programs.

I think it is important that the members of the committee understand that the FAS dismissed my 1986 inquiry as a failure on my part to understand that one of our foreign customers was merely jockeying for a better bargaining position with respect to price.

Today, both USDA's Office of Inspector General and the General Accounting Office are going to detail a wide range of abuses, management shortcomings, and compliance problems they uncovered in investigating and auditing not only the GSM-102 and GSM-103 programs, but also the Export Enhancement Program, and the Targeted Export Assistance Program.

These issues range from exorbitant profit making, anywhere from 400 percent profit on GSM sales, to what the Office of Inspector General likes to call "extra sales services," something that you and I would probably call kick-backs.

Both the OIG and the GAO have identified serious management weaknesses, including a failure to suspend and debar individuals who have committed fraudulent acts, even though the Foreign Agricultural Service has the legal authority to suspend and debar individuals who misuse programs they administer.

Ladies and gentlemen, there is no excuse for what has happened here. Programs that we in the Congress designed to help our farmers, U.S. farmers, compete, have been administered negligently, with no apology to the very individuals these programs were designed to serve: Our farmers.

It is clear that we must take action to address the various problems the Inspector General and the GAO will identify, because quite simply, FAS has demonstrated that presently it is incapable of doing so.

I have said it before, and I will say it again, the farmers deserve better than this. Congress deserves a Foreign Agricultural Service that is responsive to the problems Congress brings before it. We don't need a Foreign Agricultural Service that addresses the profit-making needs of industry at the expense of farmers.

Thank you, Mr. Chairman.

Mr. BROWN. Mr. Hopkins, do you have an opening statement?

OPENING STATEMENT OF HON. LARRY J. HOPKINS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KENTUCKY

Mr. HOPKINS. Thank you, Mr. Chairman. Let me, if I may be as direct as my colleagues and say at the outset, we are here this morning representing the farmers. We are not talking about the farmers in South America and Africa and other foreign countries. We are talking about the American farmer.

Overall, I must say that the export credit programs, in my view, have worked well. They have helped American farmers gain new markets for surplus commodities and assisted in sales increases, which have benefitted agricultural commodities raised in my home district of Kentucky.

However, through a series of hearings before the Tobacco and Peanuts Subcommittee and under the leadership of Chairman

Rose, we have brought to light abuse and fraud of these programs on the part of some exporters.

This has to stop. And these programs intended to promote U.S. agricultural products must be better managed. We are not going to settle for a continued hand-off management style or a wink and nod approach as has been the most recent experience at USDA.

In all too many instances, lax management and unsettled policy by those charged with the responsibility of administering these programs have contributed to the problem of exporters substituting foreign commodities for domestic.

Very frankly, the Inspector General's report and the General Accounting Office investigation point out serious weaknesses within USDA. As I read this report, improper oversight and faulty enforcement by the Foreign Agricultural Service have undoubtedly contributed to the troubling problems of these export credit programs.

If not satisfactorily resolved, they could threaten this program and the assistance that it provides. I appreciate the work done, Mr. Chairman, on this issue by those giving testimony before us today. I look forward to hearing the results of their efforts.

Thank you very much.

Mr. BROWN. Mr. Glickman.

OPENING STATEMENT OF HON. DAN GLICKMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. GLICKMAN. Thank you, Mr. Chairman. As chairman of the subcommittee with jurisdiction over the grains, obviously I have a great interest in the effectiveness of the Export Enhancement Program, which is the largest, in dollar amount, export program that we have in agriculture.

My objective is to make sure the program runs more efficiently with the limited resources that the Government has to give to accomplish its stated objectives. And I, like Mr. Roberts, believe that this program as well as the GSM Program have worked for our farmers, and we will continue to support these programs.

However, I believe that they can run better, and our review of these audits in preparation for writing the 1990 farm bill is critical for this.

Now, what I found most alarming about these reports is that the Office of Inspector General estimates that the USDA may have misspent as much as $115 million, solely in miscalculating bonuses awarded to exporters by understating the world price and overstating incidental costs incurred by participating exporters.

As a result of this mismanagement on USDA's part, taxpayers have spent at least $115 million more than they should have over a period of time when Congress has been required to make deep cuts in payments to farmers.

The Office of Inspector General's overall conclusion that the Export Enhancement Program has been mismanaged because it lacks guidelines and control mechanisms. It is a conclusion that we have heard in our subcommittee all along during our period of oversight in this matter.

Mr. Chairman, my questions, gut feelings and stab in the dark conjectures of neglect by the Foreign Agricultural Service have been substantiated in the OIG audit, and in the testimony we will receive from the GAO.

It solidifies my notions that guidelines directing the Foreign Agricultural Service in its bonus awards and calculations and oversight of export activities do not exist and never have existed.

Mr. Chairman, at a hearing about 8 months ago, we raised the issue of a fact that a man named Marc Rich, or an affiliate of Mr. Rich, the largest tax evader in the history of the United States of America, a fugitive from justice, indicted and convicted for trading with the Government of Iran, received $100 million in bonuses under this program.

And at that time, we said, "If Mr. Rich can get those bonuses, what else is happening in this program?" And of course, the Department is now taking steps to suspend him. I applaud them for doing that, even though they didn't act as quickly as we would like.

But the purpose of this is to figure out how we can make this program work so that it continues to serve our farmers, and wasting $115 million and providing bonuses to Mr. Marc Rich is not a way of doing that.

OIG's audit cited nine occasions where preferential deals had occurred. FAS made efforts to communicate to two importing countries price levels that would be acceptable to them in advance. This may have happened more than nine times considering that the Office of Inspector General did not evaluate all initiatives.

Notwithstanding all the other problems with the program, this kind of activity, in and of itself, may seriously damage the programs integrity and objectiveness.

Throughout this time, I do not believe the Department of Agriculture has been any more than aloof in responding to Congress about this particular program. It does not report the incredibly abundant bonuses. It is making it possible for private investors and exporters to make excessive profits on these initiatives.

In one instance, private investors made a 50 percent profit on their investment in one dairy cattle initiative. Mr. Rose has spoken about GSM.

I would just conclude by saying that this is a disturbing trend that we are seeing here. It is also a very important program. I don't want to see the program canned or cancelled, either, but I want to make sure that it works and we are not wasting tax payers dollars, and I think this hearing will serve that function very well.

Thank you, Mr. Chairman.

Mr. BROWN. Thank you, Mr. Glickman. The Chair would be willing to entertain opening statements by any other members if they feel an urgent need to do so.

Mr. OLIN. Mr. Chairman.

Mr. BROWN. Mr. Olin.

OPENING STATEMENT OF HON. JIM OLIN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF VIRGINIA

Mr. OLIN. I would like to congratulate the chairmen of the three subcommittees for having this hearing, congratulate them for

having in the beginning ferreted out and encouraged the investigation of what is very clearly evidence of gross mismanagement on the part of the USDA and the FAS.

There are, apparently, from the audit reports that I have read so far, which is not all of them, there are extensive incidents of improper payments. To what extent this involves fraud or criminal activity is not known to me at this time, but I hope it will come forward, and the total extent to which the Government has made improper and excessive payments is not yet clear to me, and I hope that it will come out of this hearing.

I hope, also, that as a result of the hearing, we will get a pretty good fix on when these things were first discovered, talked about and known about, and what actions the Department has taken since that time to correct whatever ills that might be in the picture.

Mr. Chairman, I think this is an extremely important hearing. There is evidence that much needs to be corrected, and I hope that the hearings that follow this disclosure today will eventually return these programs to what they were supposed to be.

Thank you.

Mr. BROWN. Thank you, Mr. Olin. Any other members wish to make an opening statement?

[No response.]

Mr. BROWN. If not, the Chair will call Mr. James R. Ebbitt, Assistant Inspector General for Audit, Office of the Inspector General, U.S. Department of Agriculture. Mr. Ebbitt, you have with you Mr. Craig Beauchamp, Assistant Inspector General for Investigations, and Mr. Richard Long, Deputy Assistant Inspector General for Audit.

We welcome all of you here, and you may proceed with your statement.

STATEMENT OF JAMES R. EBBITT, ASSISTANT INSPECTOR GENERAL FOR AUDIT, OFFICE OF INSPECTOR GENERAL, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY CRAIG BEAUCHAMP, ASSISTANT INSPECTOR GENERAL FOR INVESTIGATIONS, AND RICHARD LONG, DEPUTY ASSISTANT INSPECTOR GENERAL FOR AUDIT

Mr. EBBITT. Thank you, Chairmen Brown, Rose, and Glickman, ranking minority members, and members of the subcommittee.

Mr. BROWN. May I interrupt you just momentarily to say that the republican members have an urgent caucus to persuade them to vote for the pay raise, and we have excused them, but they will be back as soon as they have been persuaded. [Laughter.]

Mr. EBBITT. Thank you, Mr. Chairman. I am James R. Ebbitt, the Assistant Inspector General for Audit, and with me this morning on my left are Craig Beauchamp, Assistant Inspector General for Investigations, on my right Richard Long, the Assistant Inspector General for Audit.

We are pleased to appear before you today to discuss our audit of certain aspects of the Foreign Agricultural Service administration of three market development programs, export credit guarantee

programs or the GSM 102/103, the Export Enhancement Program, and the Targeted Export Assistance Program.

If it is acceptable with you, Mr. Chairman, I am submitting my prepared statement for the record. I have selected highlights of that statement to read to you.

Mr. BROWN. That will be satisfactory. The full text of your statement and any supplementary materials will be made a part of the record.

Mr. EBBITT. Thank you, Mr. Chairman. Regarding the GSM-102/103 Program, we have previously testified before Chairman Rose's subcommittee that commodities of foreign origin were being combined with U.S. commodities and exported under the GSM 102/103 Program. Tobacco was the product most often combined.

However, we have also found that foreign origin in vegetable seeds, beef cattle, soft drink concentrates and wood pulp were included in exports under the 102/103 Program.

These conditions are discussed in an audit report we issued in September of this year. In that report, we noted that $169 million in guaranteed sales contained foreign commodities. FAS has taken several actions in response to our audit including requiring exporters to certify that all exported commodities were 100 percent U.S. origin, clarifying nonagricultural content criteria, and suspending and debarring program violators.

Our investigation of companies allegedly including foreign tobacco in shipments of which they obtained a guarantee is continuing in coordination with the U.S. attorney's office in Raleigh, North Carolina.

We also recommended that FAS promote legislation to prevent GSM exporters from recovering import duties paid to U.S. Customs Service for imported commodities under a procedure called drawbacks.

Also, most exporters did not maintain records to show that the commodity was of U.S. origin. Without access to our records, we could not determine that a sufficient quantity of U.S. origin commodities were available in the exporter's inventories at the time of the GSM sale.

Regarding the Export Enhancement Program, we recently issued an audit report. At the time we completed our review, FAS had issued about $2.2 billion in bonuses, but had not performed a program analysis of the EEP to determine if program objectives were being met and the program costs were reasonable.

FAS had not developed written criteria for participation in the Export Enhancement Program. Therefore, we could not evaluate FAS' basis for including individual countries in the EEP, the potential impact on other U.S. markets, or FAS' response to market changes that occurred because of targeting.

Generally, countries not targeted for EEP reduce their purchases from the U.S. FAS subsequently had to target those countries to regain lost market shares.

Also, FAS targeted countries in which the European Community, the EC-12, was not a competitive factor. For example, FAS targeted Egypt for EEP in 1985, at which time the United States had 30 percent of its wheat market, and the EC-12 had no portion of that market.

Examples of targeted markets such as these suggest that a main objective of EEP, the countering of EC–12 market sharers, may not have been achieved. Specifically, the world market history shows that the EC–12 share has been constant, even after FAS implemented the EEP.

We have recommended that FAS prepare an analysis which addresses commodity and country targeting activities, the relationship of U.S. exports to those other countries, overall costs for increased market shares, and the effects of reduced ending stocks on future program activity in commodity exports. FAS has advised us that a final study has been completed, which addresses these areas.

The EEP bonus amounts are calculated using the delivered price of the commodity. As a result, the difference in cost between shipping from U.S. ports and the EC–12 ports was in the bonus calculations.

We estimate that the net effect of these adjustments was a cost of $150 million to EEP for six grain products during the period September, 1986 through August 1988. It is not clear that the Food Security Act of 1985 provided for the payment of additional shipping costs to off-set locational disadvantages.

Regarding bonus value calculations, we reviewed FAS' procedures for determining wheat prices and bonus values. FAS did not have written procedures for nor sufficient documentation to support these calculations.

Based upon available data, we believe that FAS' calculations could have overstated the bonus value by up to $2 per metric ton, resulting in a cumulative bonus overstatement as of August 1988 of about $89.8 million.

We also noted that FAS made adjustments to the bonus calculations for exporter's incidental costs. Overall, we estimate that about $25 million was overpaid in EEP bonuses for excessive incidental costs.

We have recommended, and FAS has agreed, that written policies and procedures be developed, and that FAS document any adjustments it makes to price quotes.

Regarding exporter's records, as with exporters in the GSM program, we were unable to fully assess the impact of the EEP on exporter's operations. In most cases, we could not determine an accurate profit margin on EEP sales.

In certain instances, we were able to compare exporter's estimated cost figures FAS used in its bonus calculations with the exporter's actual costs. For example, an exporter of wheat flour obtained two agreements, each to export 15,000 metric tons. The exporter estimated a shipping cost of $28.25 and $27.25 respectively per metric ton for the two agreements.

However, the exporter's records show that the actual freight cost was $18 per metric ton for both agreements. Those two agreements already contained an estimated gross margin of about $925,000. The lower actual shipping cost provided an additional bonus of $307,000.

We recommended to FAS that it change the language in its bid announcements to insure that exporters understand that they must maintain and provide records that will enable USDA officials to

analyze the financial results of the exporter's participation in the EEP.

Regarding dairy cattle, in June 1986, dairy cattle were shipped by both air and sea to destinations such as Egypt, Iraq, and Algeria. EEP bonuses ranged up to $1,800 per head. The original EEP Dairy Cattle Program, which used the bidding process to award sales was suspended because of the high cost.

In its place, FAS implemented a preannounced bonus program with stated bonuses of $700 to $900 per head, depending on destination. Had these preannounced bonus amounts been used for the initial sales, bonuses paid would have been $18 million less than they actually were.

The high bonuses made it possible for exporters to receive profit margins ranging from about 10 to 24 percent. Presently, the Dairy Cattle Program is not active. We have made several recommendations to FAS for the improvement of their management of dairy cattle exports should this program become active again.

I would now like to summarize some significant issues from our audit of the Targeted Export Assistance Program, which we issued in March 1988.

Cumulative authorized funding for the 5-year period ending September 30, 1990, is $735 million to be provided by Commodity Credit Corporation certificates. A basic principle of the TEA, as the program is commonly called, is that it is a joint effort between the U.S. Government and the participating organizations.

Specifically, the participant is expected to make a good faith effort to contribute a portion of the resources necessary to carryout the promotion activity. These contributions can come from either the participants own resources or those of third parties.

Third parties are usually private foreign companies who work jointly with the U.S. participant in managing the promotion activity in their own countries.

Our review of eight participants' records showed a lack of documentation to support third-party contributions and no documented agreements with their third-party participants to provide funding. Participants did not obtain agreements with their members for assessments to meet contributions. A participant used marketing expenses incurred by its licensees who are not participating in the TEA Program to claim and receive $2.4 million in TEA reimbursements.

After we questioned this payment, the participants subsequently repaid the $2.4 million to FAS. We also found deficiencies in U.S. participant's accounting systems, lack of documentation and established criteria by FAS to support the final funding level.

We have made recommendations for FAS to take corrective action on all of these deficiencies. Except for making participant contributions mandatory, FAS has taken corrective action on all of our recommendations. We are, however, continuing to work with FAS in a number of follow-up reviews on these issues.

We are currently reviewing the FAS compliance review staff. We are looking, again, at third-party contributions. We are looking at how FAS manages foreign debt, and we are also looking at foreign operations and currency-use payments.

This concludes my statement, Mr. Chairman, and I will be happy to answer any questions you may have.

[The prepared statement of Mr. Ebbitt appears at the conclusion of the hearing.]

Mr. BROWN. Thank you very much, Mr. Ebbitt. Mr. Rose, do you have any questions?

Mr. ROSE. Thank you, Mr. Chairman. Mr. Ebbitt, that will be the statement for you office; is that right?

Mr. EBBITT. That's correct, sir.

Mr. ROSE. Mr. Beauchamp, according to a recent article in the Wilmington, North Carolina Star News, the assistant U.S. attorney in Raleigh, working with the OIG on tobacco leaf dealer cases, admitted that he is talking with lawyers representing leaf dealers.

Mr. McCullough would not state whether a settlement was discussed during this meeting. Are you aware of the fact that the U.S. attorney in Raleigh is meeting with attorney's representing leaf dealers? Why is he meeting with leaf dealer's attorneys?

In the past, you have testified that the OIG has audited the leaf dealer's books and documented specific cases of blending, which I understand you to say, indicated fraud due to previous false statements made to the Department of Agriculture?

Mr. BEAUCHAMP. Well, Mr. Chairman, we are continuing our investigation of possible fraud relating to those sales.

Mr. ROSE. That is not my question. My question is are you aware of the fact that the U.S. attorney is meeting with leaf dealers, and why are they doing that?

Mr. BEAUCHAMP. I would not want to comment on the details of what our investigators are doing or what the U.S. attorney's office is doing. All I can say is we are continuing with our investigation.

Mr. ROSE. Well, are you aware that they are meeting with leaf dealer's attorneys?

Mr. BEAUCHAMP. I could say it would not be uncommon for either our investigators or a prosecutor in a case to discuss details with attorneys that represent certain individuals we are investigating.

Mr. ROSE. In order to curb abuses under the export programs as a matter of assuring compliance in the industry, would you recommend that these individuals or organizations, whether it is in tobacco or any other commodity, when you catch them, as you have, should they be let go with a warning? Should they be fined? Or should they be tried in a court of law with appropriate punishment?

The reason that I ask this is because I am concerned with regard to the amount of profits that the Inspector General estimated occurred with respect to particular sales, and I am wondering what is the best means to assure program compliance?

What do you think ought to happen? Should they be slapped on the wrists, given a warning? Should they be fined? Should they be tried in a court of law with appropriate punishment?

Mr. BEAUCHAMP. Well, not going to specific cases, my position as an investigator would be that if someone violates the law and is indicted for that and convicted at a trial, then the judge should give appropriate punishment.

Mr. ROSE. But you do know that USDA has the authority to suspend and debar individuals from participating in all USDA programs. I would like to know if people that you have identified as having committed fraud under GSM have been denied participation or are you just still waiting for the U.S attorney, now several years in the process, to do something?

Are you still out there doing business with these same companies that you have identified as having defrauded the Government?

Mr. BEAUCHAMP. In the case of the tobacco companies, it is our position, which we recommended to the Department of Agriculture, that they do not suspend those companies from participating in GSM programs.

Mr. ROSE. So, the Department of Justice is twiddling its thumbs, has done nothing except talk to leaf dealer's lawyers. You are still doing business with the companies that your own internal investigations say defrauded the Government. They are still participating in programs.

I find that highly irregular. I just don't understand it, and I understand that you have identified that some of these leaf dealers, who you have decided are defrauding the Government, as having blended foreign and U.S. tobacco under the GSM Program, that you have ascertained that some of these individuals process and store tobacco for the Flue-cured and burley stabilization cooperatives.

In other words, these people process Government collateral. Is that not correct?

Mr. BEAUCHAMP. Mr. Chairman, I really would not want to get into the details on what producers or what shippers are doing while the investigation is on-going.

Mr. ROSE. Mr. Long, have you ascertained whether or not these same individuals process and store Federal Government collateral?

Mr. EBBITT. Mr. Chairman, if I could please answer, some of these same companies we know store tobacco under that program. If I could just elaborate a little further, we had testified previously that the U.S. attorney had recommended in this instance that the Department not to take action to suspend of debar, pending the outcome of the investigation.

FAS did put all of these companies on notice where we found the foreign content, that should the buyers default, should there be a default in the future, and it was found that the shipment contained foreign content, that the guarantee would not be upheld.

So, the companies have been put on notice to that extent.

Mr. ROSE. Do you not have any concern about individuals processing and storing Federal Government collateral, that you have found blending U.S. tobacco with foreign tobacco and misrepresenting the origin? Any of you want to answer that?

Mr. EBBITT. Mr. Chairman, we haven't found any problems that we are aware of in the audit process regarding the storage of tobacco.

Mr. ROSE. Well, there is really no problem with a fox maintaining guard over the chicken house unless you see him eat a chicken, you understand. Then there is a problem. Now, if you are not there while he is eating chickens, a fox is a great guard for the chicken house.

But, you have fraudulent leaf dealers that you have determined have defrauded in the GSM Program, processing and storing collateral for the Commodity Credit Corporation. I find that highly irregular.

And you are saying there has been no problem so far. You haven't seen them with any leafs sticking in their mouth, to use my analogy. Is that what you are saying?

Mr. EBBITT. I don't know that I would use that analogy. So far, as it relates to other areas that these companies may be involved in with the Department, we don't have any evidence of wrong-doing.

We are proceeding as the U.S. attorney requested us to proceed in handling the case regarding the debarment and suspension, and it was his advice that the Department not take that action at this time.

Mr. ROSE. Mr. Chairman, I thank you. I have taken too long on my questions, and I would like to submit the rest of my questions for the record.

Mr. BROWN. You will certainly have the opportunity to do that, Mr. Rose, and if we get through one round, you can come back, if you wish.

Mr. Glickman.

Mr. GLICKMAN. Thank you, Mr. Chairman. First of all, I would like my colleagues to note particularly page 24 of the GAO's testimony on the EEP program where the OIG reports, referring to the testimony:

> That the Agriculture Department does not have written policies and procedures for or sufficient documentation to support world price determination and bonus calculations.
>
> Our ongoing review indicates that the Foreign Agricultural Service does not sufficiently document the specific figures used to calculate the final price and bonus levels. They do not provide either narrative or statistical support to explain how they arrived at these figures. As a result, it is difficult for an independent reviewer to determine whether bonus payments made are excessive.

Mr. Ebbitt, is that a fair statement of the essence of your report or part of it, at least?

Mr. EBBITT. Yes, Mr. Chairman, that is what we found.

Mr. GLICKMAN. Now, you state and you discuss bonus value determinations made by the FAS, and I guess I am concerned about how the Department arrived at prices that were overstating the bonus value by up to $2 per metric ton that has cost American taxpayers $89 million. Additionally, you state that an overstatement of incidental costs cost $29 million, totally $115 million or so.

Now, a couple of questions. One, does the estimate of $115 million in overcharges count for all initiatives granted at date or just a sampling of initiatives?

Mr. EBBITT. Mr. Chairman, that is just a sampling of initiatives that we reviewed.

Mr. GLICKMAN. What percentage of initiatives did you review, approximately?

Mr. EBBITT. Mr. Chairman, I don't have that readily available. I can provide that for the record.

[The information follows:]

> The initiatives included in the scope of the review of the EEP represent approximately 17 percent of the announced initiatives as of March 1988.

Mr. GLICKMAN. If you would, but again the statement is that your review was not a complete review, and therefore it is possible that there were more overcharges or problem amounts other than the ones that you found.

Mr. EBBITT. Yes, it is possible.

Mr. GLICKMAN. OK. In calculating initiatives and bonuses, the Foreign Agricultural Service needs access to a wide spectrum of information when they are doing the bonuses. How does it accumulate the information?

Mr. EBBITT. Mr. Chairman, the FAS essentially uses the services of two private sector firms, one in Rotterdam, and one in London that gathers market price data for the various countries, and they submit that to FAS, and FAS essentially uses that as the basis to begin the pricing process.

Mr. GLICKMAN. Who are those firms?

Mr. EBBITT. I don't know off-hand, Mr. Chairman, the names of those firms. We have that, and I can supply that for you.

[The information follows:]

The Foreign Agricultural Service has asked that we not publicly release the names of the firms. Should the committee need additional information, special arrangements can be made concerning the confidentiality of the information.

Mr. GLICKMAN. OK, and do you know if the companies that are supplying this information have any conflicting interests to activities going on either at Foreign Agricultural Service or any where else?

Mr. EBBITT. I don't have personal knowledge of that, Mr. Chairman. We have had some discussions with the General Accounting Office, and they have advised us that they didn't find any conflicts of interest.

Mr. GLICKMAN. It would be useful for the record to determine what these firms are and whether they have any relationships with firms that either participate in the bonuses or perhaps advise companies that participate.

Mr. EBBITT. We can provide that, Mr. Chairman.

[The information follows:]

As mentioned before, The Foreign Agricultural Service has asked that we not publicly release the firms that are supplying them with price information. They believe that release of the names would damage the objectivity of the data currently being provided to them. We share FAS's concerns on this matter. Our review did not focus on the relationships of the firms with companies participating in the Export Enhancement Programs.

Mr. GLICKMAN. Now, in your report, you state that in FAS' calculation process of a market price for an initiative, it ends up undercutting world prices in some way. Essentially, I would imagine at some point it accumulates information on world and domestic prices of wheat for that day in certain markets.

How does the FAS determine what price level is adequate for an EEP sale, and does it average them? How does it come up with a $2 understatement of prices?

Mr. EBBITT. That was part of the problem in that FAS had no written procedures to explain to us exactly how they arrived at the bottom line.

Essentially, they used the information that the private firms provided them. I don't know if they averaged it or not. They used that

data, and they took out some costs—the incidental costs that we talked about. And the $2 understatement that we note in our report, it was unexplained. We had no explanation as to why this particular $2 had been taken out.

Mr. GLICKMAN. And there is no written documentation of that?

Mr. EBBITT. That is correct, Mr. Chairman.

Mr. GLICKMAN. Obviously, we will have to follow up on that.

Now, incidental costs. You stated that we got about $29 million of incidental costs that have been given to exporters. What are incidental costs? Who decides them? Is there a list of incidental costs that are in some regulatory sheet?

Mr. EBBITT. There isn't any list that we are aware of, Mr. Chairman. One example of an incidental cost was for treatment of snow-mold on wheat grown in Minnesota and other Northern States. That allowance—I believe it included a $3.07-adjustment—was being allowed for wheat no matter where it was grown. However, if wheat was grown in Kansas where snow-mold was not a factor, that incidental cost was still being included in the bonus calculations.

Mr. GLICKMAN. Now, if exporters don't have any incidental costs, in fact does the U.S. Government get a refund from those exporters?

Mr. EBBITT. No, Mr. Chairman, that was not pursued by FAS.

Mr. GLICKMAN. So, in fact, it may have been that the incidental costs for at least some of these exporters amounted to pure profit, then.

Mr. EBBITT. That's correct, Mr. Chairman.

Mr. GLICKMAN. Incredible. One final thing, and then perhaps we will go around again. The information you include says that freight assistance in barley Export Enhancement Program to the Saudis may have been excessive. That was just one of your comments.

I have expressed an interest in one exporter, Richco, Marc Rich, who sold 25 percent of the barley EEP's to the Saudis. Do you think he received these excessive freight assistant amounts?

Mr. EBBITT. Mr. Chairman, I don't know specifically if he did or not.

Mr. GLICKMAN. Can you find that out? Is that something that is clear enough in the records?

Mr. EBBITT. We can review our work papers in the information and determine if that information is available; yes.

[The information follows:]

The scope of our review did not include any barley shipments made by Marc Rich.

Mr. GLICKMAN. Thank you, Mr. Chairman. I may submit more for the record, and if we go around, I will ask some more. Thank you.

Mr. BROWN. Mr. Grant, do you have any questions?

Mr. GRANT. Just briefly, Mr. Chairman. I understand you have just recently gotten back from Europe, and I wondered if there was any additional information that you might want to share with us that is not in your report.

Mr. EBBITT. Congressman, our auditors and investigators aren't quite back. They were delayed in transit getting back. Craig, is there anything we can comment on?

Mr. BEAUCHAMP. Not at this time; no.

Mr. GRANT. Thank you, Mr. Chairman.

Mr. BROWN. Mr. Volkmer.

Mr. VOLKMER. Thank you, Mr. Chairman. I would like Mr. Ebbitt to focus a little more on the fact that in your investigation, you say on page 3:

> Every exporter denied us access to their non-GSM records. Without access to all records, we cannot determine as sufficient commodities were available at times of GSM sales.

Is that at every instance?

Mr. EBBITT. That's correct, Congressman. Every exporter that we visited essentially would not let us have access to their non-GSM business. They would cooperate fully on providing records which they believe related to GSM sales.

Mr. VOLKMER. Now, if they did on a GSM sale, were they able to show you a full quantity of what they sold at the GSM guarantee on the commodity?

Mr. EBBITT. Congressman, they had the paperwork there to show that they could meet their commitment. That is correct. But, as far as being able to look at inventory records overall to make sure that that amount was actually available for that sale, we didn't have the opportunity to do that.

Mr. VOLKMER. In other words, you could have looked at other sales that they had made?

Mr. EBBITT. That is correct, sir.

Mr. VOLKMER. So, you are really just at their mercy for them to give you a bunch of invoices that say, "We sold 50,000 metric tons of flour to Egypt, and here is a 50,000 metric ton invoice."

Mr. EBBITT. We felt like that, yes.

Mr. VOLKMER. I understand that FAS still says that is OK, that you don't need to look at all those other records; is that correct?

Mr. EBBITT. That is essentially correct. We had recommended to FAS that they pursue this matter either by regulation or legislation, if that was required, that would provide not only the auditors and investigators, but their program people, as well, with that information so they could run the most effective program possible.

Mr. VOLKMER. Really, you can't make an audit to determine whether or not they have had that inventory of U.S.-produced commodity on-hand at the time that sale is made and when actually that sale was exported without reviewing those full records, can you?

Mr. EBBITT. That is correct, sir.

Mr. VOLKMER. Is there anybody that can?

Mr. EBBITT. No, sir.

Mr. VOLKMER. Knowing auditing procedures?

Mr. EBBITT. It is not possible.

Mr. VOLKMER. Mr. Chairman, I would like to make a recommendation that we examine—if FAS isn't going to do this—that we examine—if we are going to continue this GSM Program—and mandate it through legislation. I think it is the only way to find out by making sure that we are exporting our commodities and not somebody else's under those programs.

The other thing I would like to ask about is I understand we have paid an $1,800-bonus per dairy cattle going to Egypt?

Mr. EBBITT. When the program for dairy cattle first started, Congressman, that is correct.

Mr. VOLKMER. You know that really bogs my mind, and I am sure that anybody over there at FAS surely knows that a dairy cow doesn't cost that much. You can't find me a dairy cow worth $1,800.

Mr. BROWN. That includes first class transportation to Egypt, of course. [Laughter.]

Mr. EBBITT. FAS finally concluded that that was too high a bonus.

Mr. VOLKMER. I understand that, and they reduced it down and said, "We'll set a figure and pay $700 to $900 or something like that per cow."

Mr. EBBITT. That is correct.

Mr. VOLKMER. And that is a lot more reasonable. In general, as I review this whole thing, it appears that there isn't the internal structure guidelines, anything really in writing over there at FAS to really run these programs. Do you agree on that?

Mr. EBBITT. Yes, sir.

Mr. VOLKMER. There is no real structure in place.

Mr. EBBITT. I don't know that I would use the word structure, but I certainly would agree that procedurally there just aren't hard documented procedures that this is what you do, that this is how you determine what the bonus should be, that this is what you do to make those decisions.

Mr. VOLKMER. And also how you give oversight on it to make sure the follow-up is what you are supposed to do, and that the program is meeting its guidelines, is meeting its end, does what Congress dictates. None of that is there.

Mr. EBBITT. Let me say in regard to compliance activities, since we have issued our reports, the agency has taken some constructive efforts to increase compliance. Their review staff, in fact, has been out reviewing exporters' records to look for foreign content, things of that nature. So, there is some movement there.

But, when you get back to some of the basic questions regarding determination of bonus and how do you do that, those procedures still aren't in place.

Mr. VOLKMER. Now, there could be several reasons why this was not done. One of the reasons could be lack of manpower. In other words, you just don't have the manpower to do these things. Did you find that?

Mr. EBBITT. Mr. Congressman, we really didn't assess FAS's overall staffing to determine if they have enough manpower. They have a lot of people. They have a lot of programs they are running. I think it really falls to management to decide if they have their troops deployed correctly.

Mr. VOLKMER. Undoubtedly, there was no real attempt to set out in writing the necessary provisions and guidelines in order to arrive at the decisions that had to be made; is that correct?

Mr. EBBITT. Yes, sir.

Mr. VOLKMER. So, that is a management problem?

Mr. EBBITT. That is correct.

Mr. VOLKMER. A failure of management to do what needed to be done before they ever started?

Mr. EBBITT. That is correct, Congressman, and I would also point out that our audits were issued in September of this year. The work was actually conducted through a good part of the early part of 1989.

As you are well aware, there has been a change in management at FAS, and I would conclude that the responses we are now getting from the agency are in a much more positive vein than what we had had in the past.

Mr. VOLKMER. In other words, that they have corrected some of these deficiencies.

Mr. EBBITT. They have either corrected some deficiencies, or they are working towards procedures that will take action to correct a number of the deficiencies. And when you get back to the access to records, we are still at an impasse with the agency. They don't believe that we need that.

Mr. VOLKMER. Well, maybe we should tell them different. Thank you, Mr. Chairman.

Mr. BROWN. Mr. Smith, do you have any questions?

Mr. SMITH. Thank you very much, Mr. Chairman. Your last statement falls in one of the points that I want to make, and using the Egyptian export issue is probably the most flagrant example of what occurred when this committee directed the Congress to purchase 400 million pounds of meat and export half of it because we didn't want it floating on this market.

So, I am not trying to defend the actions of FAS, but this is a glaring example I think everybody must admit. And it may not have occurred, but I just want this committee to understand that the decision was driven by this committee and FAS was driven by this to get rid of beef. One of the ways they did it may have been in error.

The other question I have for you, this information was gathered during what time frame?

Mr. EBBITT. Well, the audit on EEP concentrated on 1988 proposals. The GSM, we also looked at 1988 with the exception of tobacco, which covered 1985 through 1988, and Targeted Export Assistance Program was back in late 1987 and early 1988.

Mr. SMITH. And of course, EEP was clear to 1986.

Mr. EBBITT. I'm sorry?

Mr. SMITH. Export enhancement went clear back to 1986. That is when this Egyptian cattle——

Mr. EBBITT. Yes, that is correct; on dairy cattle.

Mr. SMITH. So, your investigation and audit extended to what period of time in 1988, did you say? What period?

Mr. EBBITT. The work was actually being done using fiscal year 1988 data.

Mr. SMITH. Of 1988?

Mr. EBBITT. Yes.

Mr. SMITH. You were still investigating, but this audit was based upon information gathered clear back?

Mr. EBBITT. That is correct, Congressman.

Mr. SMITH. All right, then I would like to know after this audit was made public to Members of Congress and to the administra-

tion, which of these charges—let's not call them charges—which of these investigations that you have made that are critical of FAS and the Department of Agriculture have not been met by the agencies after they saw the results of the audit?

Mr. EBBITT. The one that probably stands out most is the access to records issue, both as it relates to GSM and the Export Enhancement Program.

Mr. SMITH. Let's talk about that because this committee got itself entwined in a bitter exchange with FAS regarding that very issue because some were critical of what's happening with export enhancement, and which countries are being favored with bonuses and which commodities are being favored with bonuses, and we got in such a discussion that FAS had to suspend the whole Export Enhancement Program for a time until we could kind of patch it back together.

So, the question about information is simply this: Is there a way that the Department of Agriculture, and in this case FAS, can discuss with you information regarding sensitive export opportunities for this country with other countries without that information being made public?

Mr. EBBITT. Without it being made public, yes. I would think that under FOIA procedures, if we did gain access to the exporter's records, we would also be prohibited from making those public.

Mr. SMITH. Was that offered to them through your efforts?

Mr. EBBITT. I don't think we had that kind of discussion. The discussion never really moved beyond the issue of the need to have the access.

Mr. SMITH. Well, Mr. Chairman, I guess the points have been made. I see a need for sensitive information being protected if we are going to continue this EEP program, and I for one believe we should, even protected possibly from this committee, although through executive session, this committee ought to have information that they have, but surely there is information that should not be made public for the embarrassment of not only the country we are dealing with, but this country, and under conditions that we have just discussed here.

There is no reason that the administration, in my opinion, or the Department of Agriculture, under this sort of arrangement, shouldn't give the information to the auditors. That is obvious, because if you don't do that, then you are liable to have another coverup, which we have had many too many in this country already in various other agencies of the Government.

So, I think the point is made. Thank you.

Mr. BROWN. Mr. Olin.

Mr. OLIN. Thank you, Mr. Chairman. I would like to start first with a couple of questions that relate to defining the scope of this situation. Could you give me, now, and an approximation of the amount of excessive payments that the Government has made through FAS for each of the three programs, GSM, TEA and EEP over what ever period of time you have knowledge of? You could define that yourself.

Mr. Ebbitt.

Mr. EBBITT. Under the GSM Program, Congressman, we identified $169 million in guarantees that contained foreign content. That was over the period 1985 through 1988.

Mr. OLIN. That is the total loan guarantees that were granted?

Mr. EBBITT. That contained foreign content.

Mr. OLIN. And how much of those payments do you estimate from your audit that were improperly or excessively made?

Mr. EBBITT. It would be that $169 million—all of it.

Mr. OLIN. What was the total value of the volume of loan guarantees that were made?

Mr. EBBITT. The total that we looked at, Congressman, was $500 million.

Mr. OLIN. OK, that answers that question. When you are talking about a third, it's thought to be excessive. How about the TEA with the same data?

Mr. EBBITT. I was just going to add that on that $169 million, $141 million of that was related to tobacco.

Mr. NAGLE. Would the gentleman yield?

Mr. OLIN. I would certainly yield to the gentleman.

Mr. NAGLE. Just so we are all clear on this, the $160 million you are identifying as overpayments is based only on the ones that you audited.

Mr. EBBITT. That is correct.

Mr. NAGLE. What percentage of sales did you audit?

Mr. EBBITT. During fiscal year 1988 the Department had authorization to extend guarantees of about $5 billion. There were 64 commodities that received guarantees. We zeroed in on those that had the most probability we felt for containing foreign content. And we got that list down to about 11 that we actually reviewed.

Mr. NAGLE. Of how many total sales?

Mr. EBBITT. Out of 64 commodities, those 11 contained about $500 million.

Mr. NAGLE. So, what you are telling us is that on the $500 million that you examined, $169 million amounted to overpayments; is that correct?

Mr. EBBITT. I have just been corrected. It is $1.1 billion, which was the size of the sample that we looked at.

Mr. OLIN. If I could reclaim my time?

Mr. NAGLE. I thank the gentleman for yielding.

Mr. OLIN. Let me see if I understand this. You say that in the GSM program, there was $5 billion authorized.

Mr. EBBITT. For fiscal year 1988, that is correct.

Mr. OLIN. Over this period? And the number you gave me that you estimated was in excess of $169 million or $149 million?

Mr. EBBITT. $169 million in total, Congressman. $141 million relates to tobacco.

Mr. OLIN. $141 million?

Mr. EBBITT. Yes.

Mr. OLIN. And then——

Mr. EBBITT. Could I clarify this one point?

Mr. OLIN. You can verify in a minute when I get through with this particular question. The $169 million that you think is excessive, is that the amount of the contracts that you looked into specifically?

Mr. EBBITT. Yes.

Mr. OLIN. You know that specifically?

Mr. EBBITT. That is correct.

Mr. OLIN. And you have not extrapolated that into the total volume?

Mr. EBBITT. We did not.

Mr. OLIN. The total volume was $1.1 billion?

Mr. EBBITT. $1.1 billion was the universe from which we narrowed down our review.

Mr. OLIN. Okay, what was the total volume? $5 billion was authorized. What was the total of the loan guarantees that were granted over that period?

Mr. EBBITT. It was close to the total $5 billion, Congressman.

Mr. OLIN. Close to the total. Would it be possible for you to make an estimate based on your sample of what the total excess payments would possibly be in your opinion?

Mr. EBBITT. I would hesitate to do that. Extrapolation is really a dangerous procedure to get into.

Mr. OLIN. The $169 million is a hard number.

Mr. EBBITT. Yes, Congressman.

Mr. OLIN. And with a little more investigation, you could fill that up some. The gentleman from Kansas wants to break in at this point. I would be glad to yield temporarily.

Mr. GLICKMAN. I just want to clarify. We are talking about the 169 million dollars' worth of loans were loans made on foreign agricultural products, right?

Mr. EBBITT. They were made on shipments containing foreign ag products.

Mr. GLICKMAN. And is that a violation of existing statutory authority under the GSM Program?

Mr. EBBITT. Yes, Mr. Chairman.

Mr. OLIN. Very good point. How about the excessive payments that you identified under TEA?

Mr. EBBITT. OK, under targeted export assistance, we question about $60 million.

Mr. OLIN. Yes.

Mr. EBBITT. And we had recommended recovery of $4.3 million. Actually, we asked the agency to look to determine if they needed to recover roughly $15 million. The remaining money, about $46 million, was in ways that we felt the program could have been operated more efficiently in the future, and that money could be saved.

Mr. OLIN. What was that total?

Mr. EBBITT. The total altogether was about $60 million with about $15 million in collections recommended, and about $46 million in program improvement areas.

Mr. OLIN. So, if you added the $15 million to $46 million, you would get $61 million.

Mr. EBBITT. Roughly $61.

Mr. OLIN. That is the whole amount?

Mr. EBBITT. That is correct.

Mr. OLIN. So, all of 100 percent of what you checked is really questionable. Is that a fair statement?

Mr. EBBITT. Mr. Congressman, that is the amount of what we found in error. It is not the amount that was extended under TEA.

Mr. OLIN. What was the total volume extended?

Mr. EBBITT. Mr. Congressman, I have it here in the report, if you can bear with me, or I can provide it for the record.

Mr. OLIN. Why don't you supply it for the record.

[The information follows:]

For the period under review, fiscal year 1986, $110 million was extended in the TEA Program.

Mr. OLIN. Let's get the EEP. This is the big ticket item. We are talking about total volume there of $2.2 billion?

Mr. EBBITT. Under EEP, it was $2.2 billion. That is correct.

Mr. OLIN. And what was the amount that you considered to be excessive?

Mr. EBBITT. We identified $89 million on the wheat bonus calculation and $24 million on incidental costs. That is roughly $114, $115 million.

Mr. OLIN. And how big a sample did you check?

Mr. EBBITT. Congressman, I have that, and I would be glad to provide that for the record.

Mr. OLIN. That would be fine.

[The information follows:]

To arrive at the estimated overstatement of FAS' calculated bonus values of $24.9 million, we applied the differences between the incidental costs (estimated) FAS allowed exporters A & B and the actual costs incurred by these exporters on 14 of their sales of wheat to China, Russia, Tunisia, and Morocco, and their barley sales to Saudi Arabia. The $2 per MT price difference for wheat which OIG used to calculate the estimated $89 million overstatement of bonus values was developed by comparing FAS calculated EC-12 prices for wheat for 6 days between February 1, 1988 and March 15, 1988, to price data FAS obtained from two overseas sources. OIG's analysis of this information revealed that the FAS EC-FOB prices, when compared to prices quoted by one of the sources, was less than the sources lowest price in 5 out of 6 instances. The other source was not used because the information could not be validated. Applying the $2 per MT price differential to the total number of metric tons of wheat sold (45,811,134 MTs) as of September 1988 amounted to approximately $89 million.

Mr. OLIN. Mr. Chairman, I would like to ask one more question along this line. Your audit reports here, I am reading from three reports. Only one of them has a date. That is the one of TEA, which was dated March 1988. That is report number 14-HY, and another one 18-HY on the EEP.

Does that have an issue date?

Mr. EBBITT. September 29, 1989.

Mr. OLIN. And the other report was 21-HY on GSM. Is that September, also?

Mr. EBBITT. Yes, that is correct.

Mr. OLIN. Did you have knowledge of these events that you are reporting on at an earlier date than 1986 or 1987?

Mr. EBBITT. As it relates to GSM and the EEP programs, that audit work was being conducted roughly during the early part of 1989, and culminated in our report of September.

Mr. OLIN. Did you have knowledge of these discrepancies in earlier years?

Mr. EBBITT. I guess on tobacco, Congressman, I think we actually got into tobacco in 1988.

Mr. OLIN. Were there any other reports issued by the OIG office on these subjects in the years 1986, 1987 or 1988?

Mr. EBBITT. Not on GSM or on the EEP or on TEA. TEA was released in March 1988.

Mr. OLIN. Right.

Mr. EBBITT. We did issue somewhat of a related report to the Agricultural Marketing Service on the end-user process for tobacco.

Mr. OLIN. I think I used more of my share of time on this round, Mr. Chairman. I will come back on the next round. Thank you very much.

Mr. BROWN. Thank you, Mr. Olin. I compliment you on the incisiveness of your questions. Mr. Nagle.

Mr. NAGLE. I am curious to know, when the Reagan-Bush ticket came in, there was about a 12-page report required to get food stamps every month. If you wanted food stamps, you had to fill out detailed financial data, and you had to do that every month.

Tell me what the requirements were or the depth of requirements for a person applying for an Export Enhancement Program, if you would. What kind of criteria did they have in terms of gathering information?

Mr. EBBITT. Congressman, they really didn't have any documented criteria that they could provide to us to show how they made those decisions.

Mr. NAGLE. Did they have a form to fill out?

Mr. EBBITT. There were some forms, yes.

Mr. NAGLE. But when you say forms, what were they?

Mr. EBBITT. Well, there is a variety of forms for each program for GSM or the EEP. There is a variety of forms that they use to either make their application for the guarantee, to arrange for the letter of credit with the banks to submit their proposals. All that kind of information is provided to FAS.

Mr. NAGLE. What, in your judgment, specifically would be inadequate about their initial intake process?

Mr. EBBITT. It is not so much the intake process. It is what FAS does once they have the information, and a process and a procedure they would follow to come to their decision regarding either an agreement to extend the guarantee or to accept a proposal under EEP.

Mr. NAGLE. Now, in the areas that you have identified of overpayment, has the FAS taken steps to recoup the money?

Mr. EBBITT. On the targeted export assistance, they have. Under EEP, they have not. Under the GSM, of course, the investigation is continuing as it relates to tobacco, so that action is essentially on hold.

On some of the other commodities under GSM, they have rescinded the guarantees.

Mr. NAGLE. Under the EEP they have not?

Mr. EBBITT. That is correct. They have not.

Mr. NAGLE. What rationale is there for that?

Mr. EBBITT. I guess looking at it from their standpoint, they were satisfied with the bonus level that was extended. So, they have already entered into an agreement with the exporter, and agreed to what the bonus will be. I don't know that they would ever go back and ask for recovery, particularly as it relates to that $2 situation

with the wheat because that wasn't an area where the exporter failed to provide information. It was simply the fact that FAS doesn't have documentation to explain why they backed off the price $2 more.

Mr. NAGLE. So, within the EEP program, if you can get away with it, you keep it, basically. If you make the sale and they overpay, you get to keep the money under the current modus operandi over there?

Mr. EBBITT. They haven't made any attempts to go back and collect.

Mr. NAGLE. OK, go ahead. The people under the tobacco investigation, are they still being allowed to be eligible for the program and continue to make sales?

Mr. EBBITT. They are still operating in the program; yes.

Mr. NAGLE. If we wanted to know the full extent—to pick up where Mr. Olin was going—the full extent of overpayments, would it literally require an audit of all sales made since the inception of the program?

Mr. EBBITT. If you wanted to determine down to the last dollar, that is correct. You would have to look at every proposal. On GSM, you would have to revisit every exporter to determine if you have foreign content or not.

We believe that we have gotten, particularly on GSM, that we have really gotten into those commodities that had the best potential to include foreign content, and that we did take a very good look at that area.

Mr. NAGLE. What about EEP?

Mr. EBBITT. On EEP, we essentially did a sampling of proposals. We concentrated mainly on wheat because wheat constitutes about 67 percent of the bonus paid under EEP. So, our review was, for the most part, directed toward wheat.

Mr. NAGLE. But you did not—and I am not critical because you are doing an audit—but you did not review all the sales, just a percentage of the sales.

Mr. EBBITT. That is correct.

Mr. NAGLE. And, so if we wanted to know the extent of the overpayments on the EEP, we would have to review each sale.

Mr. EBBITT. That is correct.

Mr. NAGLE. If we reviewed each sale, would it be possible to determine whether or not there were overpayments?

Mr. EBBITT. If you reviewed every sale, you would be able to identify whether or not you have problems on the incidental cost and world price issues. You could look again at the agreed upon bonus based upon the world market price at the time of the sale.

So, you could make those individual judgments.

Mr. NAGLE. If we did that, would we start to see the emergence of a pattern, or did you in your audit see an emergence of a pattern of specific companies that seemed to be consistently receiving overpayments?

Mr. EBBITT. We did not identify that.

Mr. NAGLE. You did not identify the companies?

Mr. EBBITT. We did not identify any patterns among companies or in the awarding of the bonus.

Mr. NAGLE. You mean all companies were equally eligible for the overpayment?

Mr. EBBITT. All companies were handled by FAS in the same fashion.

Mr. NAGLE. I yield back, Mr. Chairman. Thank you.

Mr. BROWN. Thank you, Mr. Nagle. Mr. Rose.

Mr. ROSE. Thank you, Mr. Chairman. Page 22 of your audit report, you state:

> Also we have become aware of other potential problems in the GSM other than overpricing since the completion of our field work on this audit.
>
> These problems include such things as the potential for guaranteed loan funds being returned to the purchasers, and exporters' selling price could be in line with current market transactions and still return funds to a buyer by just accepting a lower profit margin on the transaction, and exporters' GSM file may contain documentation to indicate such an action has taken place.

Gentlemen, what are you trying to tell us, that there are kickbacks in the GSM Program? Would you illustrate what you mean by these sentences?

Mr. EBBITT. Mr. Chairman, what we have noted during that review process, we have one example in the wood pulp, where the foreign buyer asked for and received a 1 percent add-on in lumber over-and-above the agreed upon sales. So, in other words, he said in order to make this sale, I want an additional 1 percent.

We also have been made aware of, and FAS is aware of, other cases.

Mr. ROSE. Did you ever find any evidence in at least one exporter's files that part of the contemplated GSM transaction included air conditioners, tires and other industrial products in addition to the requested agricultural commodity, and has the GAO identified, at least for you, one transaction where a customer received additional tobacco for agreeing to withdraw his complaint about the foreign content of the shipment he received?

Mr. EBBITT. As it relates to the first part of your question, we do have evidence of the importer requesting mechanical parts, tires—that kind of—air conditioners; yes, Mr. Chairman, and that is where it was finally agreed upon that the increase in the lumber as opposed to those items.

I am aware of what GAO has noted regarding the settlement on that tobacco case.

Mr. ROSE. Does the Foreign Agricultural Service know that items other than U.S. ag commodities—for example, tires and air conditioners—were requested by foreign customers, and how does FAS plan to address this problem?

Mr. EBBITT. FAS has become aware of those requests, and particularly as it relates to Iraq, most recently, and their position is that they strongly discourage that kind of a business position, and they have told us that they have received agreements from Iraq that those requests will stop.

Mr. ROSE. Are they violating any law other than laws against fraudulent statements to the Federal Government when they do these things?

Mr. EBBITT. I am not clear on that, Mr. Chairman. I think really the Department's attorneys or the Justice Department will have to review the legality of those kinds of agreements.

Mr. ROSE. I understand certain issues have arisen with respect to the fact that certain banks handle the majority of certain export credit guarantee sales. What can you tell us about this, and is the U.S. attorney in Atlanta investigating this matter?

Mr. BEAUCHAMP. Mr. Chairman, if I can respond to that, we have an inquiry concerning one bank in Atlanta concerning GSM guarantees. We have that under investigation right now, but it would be too early to say one way or another if there is any problem related to the GSM guarantees.

Mr. ROSE. Your GSM audit reflects a finding on your part that profits realized by exporters to the commodities surveyed range from a high of 420.13 percent profit to a low of minus 0.19. I might add that the minus 0.19 profit does not reflect any profit related to the use of drawback or customs duties.

Are you telling us that the 420 percent profit is a reasonable profit when it does not distort the GSM Program guidelines, or are you suggesting that a certain profit margin inhibits the effective operation of the Export Credit Guarantee Program?

Mr. EBBITT. Mr. Chairman, we didn't make a recommendation that would ask FAS to set up profit ranges. We didn't feel it was necessary.

Mr. ROSE. But, it would certainly occur to you that if somebody was making a 420-percent profit that this might not be the kind of sale that should go under GSM, would it not? That it might sort of stand of its own feet. It wouldn't be one of those close calls, would it?

Mr. EBBITT. Mr. Chairman, that is what we concluded in our audit report.

Mr. ROSE. And did you recommend that to FAS, and did they say, "We're going to set up some guidelines to kind of just help the marginally greedy?"

Mr. EBBITT. We made two recommendations. One was that they get us access to records, and second, that FAS do a price review as these proposals come in. FAS has agreed to the price review.

What they are trying to do is to have the GSM sale be in line with non-GSM sales. So, in other words, if a sale price is reasonable on the non-GSM side, that is what they would expect to happen on the GSM side. That is what they are shooting for.

Mr. ROSE. Thank you.

Mr. BROWN. I would like to recognize the two members who have come in and haven't had a chance to ask any questions if they would like to ask any questions at this point. Mr. Tallon?

Mr. TALLON. Mr. Chairman, I don't have a question at this time. I just congratulate you and Chairman Rose for trying to get at the bottom of a very serious matter. Thank you.

Mr. BROWN. Mr. Penny, do you have any questions at this point?

Mr. PENNY. Mr. Chairman, I am not sure what to say other than I am getting fed up with the corruption, the fraud, the misuse of public funds, the inept administration that has been a part of so many programs and agencies under the Reagan administration. This is just another example of this kind of misuse.

And I can't believe that a Republican administration, which ought to have some good business instincts and some good business

executives coming in to work for it, would allow this kind of thing to happen.

I appreciate the fact that this has been brought to light, but it just gets a bit tiresome when week after week we see one more example of a program that has been poorly run, of money that has been wasted. We have red ink drowning us here in Washington, D.C. Better management of these programs isn't going to solve all of our budget problems. But it would help.

It is just inexcusable to have this kind of waste evident in so many Departments and agencies. You can be sure that this committee is going to have a strong interest in cleaning up the messes that are evident in the programs and services that are under its jurisdiction, and we are going to need all the help we can get from honest and decent public servants in helping to root this out and put an end to it.

Mr. BROWN. Thank you, Mr. Penny. Mr. Grandy.

Mr. GRANDY. No questions, Mr. Chairman.

Mr. BROWN. All right, we will get back to Mr. Glickman.

Mr. GLICKMAN. First of all, I want to echo Mr. Penny's statement, and I don't think he was criticizing you, Mr. Ebbitt, but I think that there was clearly criticism of the Department that was justified.

Not only does FAS have inadequate guidelines to implement these programs, but its oversight activities have been limited not only because it doesn't do it, but participating exporters themselves have not been required to maintain or submit information which reveals profits and losses or practices or experiences in these programs.

Is that correct?

Mr. EBBITT. That is correct, Mr. Chairman.

Mr. GLICKMAN. So, the FAS does not want to, for whatever reason, require exporters to submit nonprogram financial information for purposes of determining compliance. Therefore, the exporters could be walking away with millions of dollars or cheating the program, and nobody will know. That is the purpose of having this kind of oversight, documentation, and I think the testimony of the OIG states that there is no documentation of what these people are doing.

There isn't a fox or a chicken in this particular situation, I would tell Mr. Rose. Now, you stated that it was hard for you to determine all of your findings because of this lack of documentation; is that correct?

Mr. EBBITT. That is correct.

Mr. GLICKMAN. And when you specifically asked exporters to provide this information, they told you that it was impossible to track because profits and losses are integrated systemwide; is that correct?

Mr. EBBITT. That is correct.

Mr. GLICKMAN. I just can't believe that exporters do not maintain information on their profits and losses in these programs. It is like a car dealer not keeping records on how much he profits from selling cars or even a certain kind of car in a given year.

Second, I can't believe that any agency running Government programs involving so much money would not require participants or

really beneficiaries—these people are making money—to maintain and submit separate EEP as well as GSM and TEA documentation on their profits and losses and other pertinent business.

Furthermore, it should be a requirement to submit nonprogram financial information for purposes of compliance reasons. Now, why is FAS opposed to this latter point?

Mr. EBBITT. FAS has essentially taken a stand that they believe it is a private deal. It is a private deal, and that is how they want to look at it. They want to provide the oversight, but once they agree up front that this is what they are going to do, they believe it is a private deal to be carried out.

They want to put the control on the front end on the price-review activity. In other words, if it appears that this is in line with private sector deals of a similar nature, that is where they want to put their emphasis. It is not after the fact. It is not a review after the fact.

Mr. GLICKMAN. I would be glad to yield to Mr. Nagle.

Mr. NAGLE. I am just curious, and I raise this with some hesitancy, but do we know by name who the companies are?

Mr. EBBITT. We know the names of the proposals and the companies involved; yes, Congressman.

Mr. NAGLE. And do we know the officers of those companies?

Mr. EBBITT. I am sure that that is available.

Mr. NAGLE. Have we run any correlation between the beneficiaries of these overpayments and their political activity?

Mr. EBBITT. No, Congressman, we have not.

Mr. NAGLE. Would that be an appropriate area of inquiry?

Mr. EBBITT. We normally wouldn't do that, Congressman, unless we had an allegation of wrong doing or something along that line.

Mr. NAGLE. Does a 420-percent profit raise kind of a question of wrong doing?

Mr. EBBITT. I would point out on that one that obviously that was the extreme in the cases that we looked at, and it certainly raises a question regarding the transaction.

Mr. NAGLE. I would suggest, it would seem to me, to clear the air, whether it is a case of mismanagement or a case of HUD II, that an inquiry be made as the recipients and the relationship to the administration. Wouldn't that be an area of proper inquiry.

Mr. EBBITT. We can take a look at that, Congressman.

Mr. NAGLE. Would you do so?

Mr. EBBITT. Yes, sir.

Mr. NAGLE. I thank the gentleman for yielding.

Mr. GLICKMAN. I have no further questions other than commenting that in the GAO report, they have a lot more amplification of this particular issue of FAS requirements, exporter controls, that kind of thing that the record ought to note.

Thank you, Mr. Chairman.

Mr. BROWN. Mr. Olin?

Mr. OLIN. Thank you, Mr. Chairman. On the point that Mr. Nagle was raising, in your audit reports, all of the individual companies are listed by company A, B, C and so on, and then you referred to various exhibits.

Would a simple request by this committee be sufficient to make available to us the names of those companies?

Mr. EBBITT. Yes, Congressman, we can do that. Typically, when we issue these reports, we don't name companies, but we can provide that list to you.

Mr. OLIN. And the exhibits would be available to us, also?

Mr. EBBITT. Yes, Congressman.

Mr. OLIN. I think in this case it will be highly desirable to have that information because of the sensitivity of it and the magnitude of it.

Mr. BROWN. We will make that request to you. Do you need that in writing?

Mr. EBBITT. No, Mr. Chairman, we can accept that.

Mr. BROWN. All right.

Mr. OLIN. Mr. Chairman, this would be the exhibits that accompanied the audit reports, plus the code names for each of the companies. Please mail your response to my office, if possible.

Mr. EBBITT. I believe, Congressman, the exhibits are attached to the report. Everything should be there. We can identify the listing of the companies.

Mr. OLIN. The committee may have that. I don't happen to have it.

Let me ask just one more series of questions. On this subject of the intermixing of foreign commodities or agriculture items with the domestic and then exporting it and getting the drawback. I take it this occurred in volume principally in tobacco, but that it also involved beef cattle, seeds, soft drink concentrates, wood pulp.

Your report also says that FAS' policy has always been to guarantee only U.S.-origin commodities in shipments. But that occasionally it had allowed foreign-origin commodities to be included.

How is it conceivable that the FAS would not have been sensitive to the possibility of foreign items being included in these exports?

Mr. EBBITT. I would point out, Congressman, that again, particularly as it relates to tobacco, where that problem was most evident, the companies essentially didn't tell the truth to FAS when they applied for the guarantee. They stated on all the documents submitted that it was domestic production.

FAS told us that it has always been their policy to extend the guarantee only for domestic production.

Mr. OLIN. Was that policy a matter of law or is it a matter of their rulemaking?

Mr. EBBITT. As I understand it, Congressman, it was a matter of law. However, the Department, as we have testified before, has allowed shipments to contain foreign content with the understanding that the guarantee would only be extended on the domestic portion of the shipment.

The CCC Charter Act, Commodity Credit Corporation Charter Act, makes it clear that the guarantee can only be extended on domestic commodities.

Mr. OLIN. If those cases that you described where they had known mixture, but they tried to confine our involvement to the domestic content, were any of those shipments tobacco shipments?

Mr. EBBITT. Yes, Congressman.

Mr. OLIN. And so, how is it reasonable to suppose that the FAS was not aware of the possibility of mixed shipments in the case of tobacco?

Mr. EBBITT. I am not sure that I am following the question.

Mr. OLIN. You said that the principal reason for these mixed shipments having occurred was that the exporters lied to the FAS. That is what you are saying. But, if the FAS had prior experience with mixed shipments in the tobacco industry, would you not expect that they would be a little suspicious in that area?

Mr. ROSE. Would the gentleman yield?

Mr. OLIN. I certainly would yield.

Mr. ROSE. I see where he is headed. The confusing part here is that you haven't explained to him that the FAS has changed its position on this matter, and that at one time they told the committee, our committee, that they only accepted U.S.-grown commodities and only would have a guarantee on U.S.-grown commodities, and the whole shipment had to be U.S.-grown commodities.

And then they came back and said, "Oh, no, we had a policy that said if part of it was U.S. grown, we would accept a guarantee on that portion of it." But the GAO, as I recall—my staff should correct me on this, Heidi—is that the GAO found no evidence of that in the files anywhere.

Isn't that correct?

Mr. EBBITT. That is correct, Mr. Chairman.

Mr. ROSE. And so, Mr. Olin, the main problem here was lying to the Government by certifying that the shipment was all U.S. grown when it was, in fact, a mixture.

Your question is absolutely correct, though. If they had, in fact, been accepting mixed shipments and taking a guarantee on a part of it, then they certainly would have known that there was blending.

Mr. OLIN. That is what the language in this report seems to indicate, does it not, Mr. Ebbitt?

Mr. EBBITT. Well, again——

Mr. OLIN. I am talking about your audit report number 21-HY.

Mr. EBBITT. Again, we reported that the main problem was the exporter incorrectly certifying to FAS——

Mr. OLIN. I understand that, but I am talking about the statement that the FAS had a policy of 100 percent U.S., except that at some time in the past, they had the policy of allowing some mixed.

Mr. EBBITT. That is correct.

Mr. OLIN. And that involved tobacco shipments.

Mr. EBBITT. That is correct, except that——

Mr. OLIN. They knew that that practice was going on in that industry.

Mr. EBBITT. They told us that they allowed that practice, but as Mr. Rose was just indicating, and as we and GAO also found, we could find no evidence where a shipment of that nature had ever been approved by FAS.

So, in other words, they told us they had the policy to allow that kind of a mixed shipment with the guarantee only on the domestic portion, but we could find no evidence where a shipment of that nature had actually been approved and gone out.

Mr. OLIN. Shipment of what nature?

Mr. EBBITT. That contained both foreign and domestic content and the guarantee only being allowed on the domestic portion.

Mr. OLIN. You did not find such a shipment?

Mr. EBBITT. That's correct.

Mr. OLIN. But you did find that the FAS was knowledgeable of the fact that there were such shipments.

Mr. EBBITT. They told us that, but there was no evidence in their file that they had ever approved a guarantee for that kind of a shipment.

Mr. OLIN. Would you be willing to go back and ask some more questions on this subject and clarify that point for us?

Mr. EBBITT. I would be happy to, Congressman, but unless I am misunderstanding the question, I think that issue is clear.

Mr. OLIN. I would be very happy to supply a carefully worded question, that maybe it would be clear enough.

Mr. EBBITT. Fine.

Mr. OLIN. If you could respond to that when you get it. You can send the response to my office.

Let me ask a question on one more subject here. On the subject of the dairy cows, there were no incidents of the mixing of European and domestic dairy cows in shipments, or were there?

Mr. EBBITT. No, Congressman, we didn't find that under the GSM Program, we found Mexican cows coming into the United States, being fed here in the United States, and then reexported to Mexico.

Mr. OLIN. Under this EEP program?

Mr. EBBITT. No, under GSM.

Mr. OLIN. Under GSM?

Mr. EBBITT. Yes. Under EEP, we did not find.

Mr. OLIN. OK, you have referred to beef cattle, but that included some dairy cattle?

Mr. EBBITT. The dairy cattle issue relates to the EEP Program and the beef cattle relates to the GSM.

Mr. OLIN. I will study that a little bit more. One statement you made here that I wanted to ask about, you have a lot of data about the size of the EEP in the case of dairy cattle, and it has been commented on, and it is pretty high. And you have a section here in your audit that says they talk about three principal exporters that you investigated that accounted for a pretty good hunk of the volume.

Then you said, "These three exporters were selected for review because they had unresolved issues pending with FAS." What were those issues?

Mr. EBBITT. They essentially were appeals of the bonus. It was at that time when FAS said, "Wait a minute, this bonus level is too high," and they wanted to, in effect, renegotiate, and these companies were appealing those decisions.

Mr. OLIN. I was aware at the time that FAS was complaining about the high bonuses. In fact, it came to the point where they shut off the dairy activity because of that.

Mr. EBBITT. That's correct.

Mr. OLIN. Thank you very much. I may have a number of questions, Mr. Chairman, to submit later on.

Mr. BROWN. We will hold the record open for any written questions that members would like to submit. We would appreciate your help in answering them.

I would like very much to get on to the GAO unless a member has an important question like Mr. Volkmer does.

Mr. VOLKMER. I will make it fast. Of those exporters who had certified that they had certified American tobacco in the mixed shipment. Were any of those repeats?

Mr. EBBITT. Where companies had certified——

Mr. VOLKMER. In other words, done it more than once?

Mr. EBBITT. Yes, Congressman.

Mr. VOLKMER. And yet, those same people are still not debarred from further contact.

Mr. EBBITT. That is correct.

Mr. TALLON. Mr. Chairman.

Mr. BROWN. Mr. Tallon.

Mr. TALLON. Thank you, Mr. Chairman. Mr. Beauchamp, you may have some reservation in getting involved in this line of discussion. How much fraud was involved here when we are talking about dollars? I have seen $141 million talked about as the dollar amount involved in this.

Mr. Ebbitt, I see you nodding your head.

Mr. EBBITT. Well, the $141 million directly related to tobacco shipments, and then there was an additional $28 million to get to a total of $169 million identified overall.

Mr. TALLON. Mr. Beauchamp, that is very serious fraud. What have you recommended to the Justice Department? What has the Office of Inspector General recommended to the Justice Department?

I think these people ought to go to the penitentiary. They have stolen from the American taxpayer. They have stolen from American producers. Is there some plea bargaining going on?

Mr. ROSE. Would the gentleman yield?

Mr. TALLON. Yes.

Mr. ROSE. If it winds up that they just get a warning letter, will you be upset?

Mr. TALLON. I will be extremely upset.

Mr. ROSE. I will, too. Thank you.

Mr. TALLON. Seriously, what have you recommended? What is going to happen here? What is the bottom line? What is going on? We know fraud is going on, but what are we going to do with these people?

Mr. BEAUCHAMP. Congressman Tallon, all I can say because it is an ongoing investigation is that we believe it is a serious matter. That is why we opened up the investigation, based on information from the previous audit and from your subcommittee.

At this point, we aren't recommending anything. We are still conducting the investigation.

Mr. TALLON. But we are talking about $141 million in this tobacco business fraud. We are talking about defrauding the American taxpayer and the American producers.

Now, you need to go back and recommend that these people be put in the penitentiary for this. I am serious. I don't know why you haven't recommended anything, but you need to get involved in this thing. We don't want to see any plea bargaining going on here.

Mr. BEAUCHAMP. Congressman, I know what you are saying. Really, all I can say is because it is an ongoing matter, I can't really say much more than that.

Mr. TALLON. Well, listen, don't disappoint us now.

Mr. BEAUCHAMP. This is the fourth time I have been testifying on it, and I imagine there might be a fifth or a sixth.

Mr. BROWN. Mr. Nagle.

Mr. NAGLE. Can I take you into an area that you haven't talked about, or at least I haven't heard you talk about. There is currently pending a request for an export enhancement for the sale of value-added U.S. vegetable oil to the Soviet Union, and I noticed that you raised some questions with regard to the decisions of the administration of this program with regard to how they pick their targets.

Mr. EBBITT. That's correct.

Mr. NAGLE. Did you find that there was a decision made on the basis not of the merit of the proposed sale, but the basis of the State Department interfering or objecting to the sale of our products to the Soviet Union?

Mr. EBBITT. Congressman, we didn't find that. The record was not clear frequently as to why decisions were made, but we didn't find that as the reason.

Mr. NAGLE. Did you, in the course of your investigation or your audit, did you review proposed U.S. sales to the Soviet Union of agricultural products that were turned down?

Mr. EBBITT. I don't believe we did, Congressman. We can review our file and see. Essentially, on that targeting issue, we were looking at why did FAS target the country. What documentation did they have as a reason to target a country.

Mr. NAGLE. And what did you find in terms of documentation?

Mr. EBBITT. We found it seriously lacking. There was little explanation there that an auditor could review as to how or why they came to their determination.

Mr. NAGLE. Did you see any correlation between the denial of a sale to a company and the subsequent sale by a Third World country with a substantial foreign debt?

Mr. EBBITT. We didn't draw that correlation, no.

Mr. NAGLE. Did you not draw that correlation because it was not there, or you didn't look at it?

Mr. EBBITT. We didn't review that area.

Mr. NAGLE. Thank you.

Mr. BROWN. Gentlemen, we thank you very much. Obviously, there is a great deal of interest in the committee, and we may have some additional questions in writing, which we hope that you will be able to respond to, but we think you have done an excellent job this morning.

You want to say something?

Mr. ROSE. I want to thank you, and when we get upset—I know it goes with the territory—we aren't upset at you. We are upset at the process that is going on. Mr. Glickman is ready to summon the high muckety-muck down at USDA, and have at him for a while, and we might get you all to come and kind of hold his shirt for him.

But thank you very much for a great job.

Mr. EBBITT. Thank you, Mr. Chairman.

Mr. BROWN. Thank you, gentlemen, and we will now call the GAO representatives, Mr. Allan Mendelowitz, accompanied by Mr. Phillip Thomas.

Mr. Mendelowitz, we appreciate the fact you have been kept waiting here quite a while this morning, and we apologize for that. We will try and be a little more expeditious with you, and you may present your statement in any way that you wish. If you care to abbreviate it in any way, the remainder of it will all appear in the record, as you know.

STATEMENT OF ALLAN I. MENDELOWITZ, DIRECTOR, TRADE, ENERGY, AND FINANCE ISSUES, NATIONAL SECURITY AND INTERNATIONAL AFFAIRS DIVISION, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY PHILLIP J. THOMAS, ASSISTANT DIRECTOR, AGRICULTURAL TRADE ISSUES; JANET PIETROVITO, PROJECT MANAGER, TARGET EXPORT ASSISTANCE PROGRAM AUDIT [TEA]; JULIE GERKINS, PROJECT MANAGER, EXPORT ENHANCEMENT PROGRAM AUDIT [EEP]; AND SCOTT EINHORN, PROJECT MANAGER, GSM 102/103, EXPORT CREDIT GUARANTEED PROGRAMS AUDIT

Mr. MENDELOWITZ. Mr. Chairman, I would be very happy to read a short summary statement and submit the full statement for the record.

Mr. BROWN. And would you introduce the rest of your colleagues?

Mr. MENDELOWITZ. I would be very happy to do that. On my right is Mr. Phil Thomas, who is our Assistant Director for Agriculture Trade Issues, and to his right is Mr. Scott Einhorn, who is Project Manager on the work we are doing on the GSM 102/103 Program. On my immediate left is Ms. Julie Gerkins, who is the Project Manager on our work on the Export Enhancement Program (EEP), and to her left is Ms. Janet Pietrovito, who is Project Manager for our work on the Targeted Export Assistance Program.

Mr. BROWN. We are happy to have you all here, and we hope that this won't be too strenuous on you.

Mr. MENDELOWITZ. Mr. Chairman and members of the subcommittees, we are pleased to be here today to discuss with you the status of our ongoing work on several programs administered by the Department of Agriculture's Foreign Agricultural Service.

With respect to the Targeted Export Assistance Program, we are reviewing the extent to which FAS has implemented the recommendations made in our May 1988 report on TEA.

Since that time, FAS has made some improvements, particularly more broadly advertising the program and in formalizing its application procedures. It has also established an evaluation branch and charged it with the responsibility for clarifying evaluation requirements, working with the commodity divisions, and tracking evaluations themselves.

Our current review has shown, however, that FAS still does not have an adequate system of internal controls to effectively manage the program. Guidelines for the program are not clearly understood by participants, and several have expressed confusion in such

areas as contracting out, authorized expenditures, contributions and evaluation requirements.

Minimal documentation exists on major program decisions leaving FAS vulnerable to questions of accountability and fairness. There is little coordination of funding and activities between the TEA Program and the Cooperator Foreign Market Development Program, even though approximately half of the TEA participants also participate in the Cooperator Program.

FAS exercises only minimal oversight over the program. To date, the new evaluation section has done little to track and analyze evaluation results, and it is not planning to evaluate the success of TEA overall.

Based on our work to date, we believe there may be an opportunity for FAS to better utilize its resources and improve the management of its market development programs. By combining the TEA and Cooperator programs, FAS would be in a better position to more effectively manage its programs and make more efficient use of its limited staff. This is an issue we are currently pursuing.

With respect to our review of the Export Enhancement Program, we are looking at three major areas: EEP program activity, external effects and administration.

The EEP has contributed to increased U.S.-agricultural exports, particularly wheat in many countries, including the Soviet Union, China and those in the Middle East. The extent of its contributions, however, is difficult if not impossible to quantify because of the many factors that influence exports.

Although in its early years, the EEP increased the cost of subsidies for the European Community, it has neither deterred the EC from using subsidies nor hurt its share of the world market.

Nevertheless, we believe that the EEP has been instrumental in bringing the EC to the negotiating table, and as such should continue as an important trade policy tool until such time as agreements are reached on reducing agricultural export subsidies.

The effects of EEP are being felt by other U.S. competitors, specifically Australia, Argentina and Canada. While EEP was designed to challenge subsidizing competitor nations, particularly the European Community, the above-mentioned countries have been adversely effected, both in terms of lower prices for the commodities and reduced market shares.

Administration of the EEP is a complex and cumbersome process. While FAS staff has been working to improve the process, a number of problems remain unresolved. For example, FAS processes each EEP targetting proposal through one of three divisions depending on the commodity. FAS does not have a central point where proposal progress is documented and controlled from submittal to approval or rejection.

Price and bonus calculations are not accurately documented. It is currently difficult to determine from the available records whether bonus payments have been excessive.

We also identified eight bonus overpayments totalling more than $635,000, which resulted from weaknesses in internal controls over the issuance of generic commodity certificates. Better controls would help insure that exporters do not receive bonuses in excess of the amounts allowed by the contract agreements.

The EEP remains an important trade policy tool because unilaterally abandoning it would weaken the U.S. negotiating position with the EC. In today's tighter wheat market, the EEP is appropriately being used more selectively.

However, in light of the large continuing EC export subsidies, it is important to fund EEP at levels adequate to maintain the program's credibility as a trade policy tool. If market conditions change, the EEP could again be used aggressively, potentially increasing the cost of the EC subsidy program and applying pressure on others to negotiate.

With respect to the review of the GSM 102/103 export credit guarantee programs, we have reported on these programs of the Commodity Credit Corporation several times over that past several years. Each time, we have discussed a need for improved program management.

Today, I am pleased to say that FAS officials have taken some action on our concerns. However, we believe more needs to be done. FAS officials are now more accurately accounting for outstanding guarantees, and they are reviewing applicants' compliance with program regulations.

Other ways to improve management of the program would include physically verifying that only U.S.-agricultural products are being exported, as required, taking suspension or debarment actions when circumstances dictate, better defining commodities that are eligible for program coverage, and improving the timely handling of revisions to GSM documents when requested by program participants.

Since we last reported on the GSM programs, a major participating financial institution has become embroiled in controversy over its unauthorized loans to Iraq. Many of these loans are guaranteed for repayment under the GSM Program.

In light of the circumstances surrounding the controversy, we believe that the FAS may want to take a hard look at the extent to which individual financial institutions participate in the program and assess the potential impact that such participation may have on CCC's guarantee liability.

This concludes my summary statement. We are providing, as we agreed, the full statement for the record, and we will be happy to try to answer questions you may have.

[The prepared statement of Mr. Mendelowitz appears at the conclusion of the hearing.]

Mr. BROWN. Thank you very much, Mr. Mendelowitz. Mr. Rose.

Mr. ROSE. Thank you very much, Mr. Chairman. I think you have heard when OIG estimated the extent of the fraud that has been uncovered. I don't think it is necessary to repeat that.

Do you generally agree with their responses to those questions?

Mr. MENDELOWITZ. We do.

Mr. ROSE. OIG's audit report states that USDA has suspension and debarment authority with respect to the GSM program where an individual has committed fraudulent acts.

Is there any question in you mind that USDA has the legal authority to suspend and debar individuals who have violated USDA program rules and guidelines?

Mr. MENDELOWITZ. We believe that the Department of Agriculture clearly has the authority to suspend and debar participation in these programs of individuals who have violated USDA program rules and guidelines.

Mr. ROSE. And that extends to all USDA programs, does it not?

Mr. MENDELOWITZ. We believe that is the case.

Mr. ROSE. We know that the OIG has identified certain leaf dealers as having blended foreign and U.S. tobacco under the GSM Program. We know that according to program rules and guidelines that the blending was wrong.

Have you ascertained whether or not any of the individuals at OIG has identified as having blended foreign and U.S. tobaccos under the GSM Program also process and/or store Federal Government collateral? Government collateral, in this question, relates to tobacco taken under loan by the respective Flue-cured stabilization and burley cooperatives.

Mr. MENDELOWITZ. Yes, we have. That is the case.

Mr. ROSE. And do you have any concerns regarding any individuals who process and store Federal Government collateral at the same time they failed to follow other USDA program rules and guidelines?

Mr. MENDELOWITZ. All these programs have substantial public resources involved in them.

Mr. ROSE. I beg your pardon?

Mr. MENDELOWITZ. All these programs involve the provision of substantial public resources to private sector individuals, and I think that we are troubled by the fact that you have participants under some programs violating rules who also have responsibilities under other programs at USDA.

Mr. ROSE. Just for those who might not understand it, what we are talking about here is the same leaf dealers that OIG has identified as having made fraudulent statements to USDA regarding GSM shipments also operate redrying plants, where they take tobacco that is destined for the stabilization cooperative as an agent of the Commodity Credit Cooperation to be collateral under the tobacco loan program.

These same leaf dealer/processors are processing this tobacco, storing it, and keeping it as collateral for the loans that were advanced to farmers.

Mr. MENDELOWITZ. That is correct.

Mr. ROSE. I am afraid that this problem is going to go much deeper than what we are talking about here today before it is over, but we are hinting at the outskirts of it anyway.

I understand that you staff traveled to several foreign countries for the purpose of visiting with foreign customers who participate in the Export Credit Guarantee Program. Did any individual you spoke with in Iraq tell you that the matter of blending foreign and U.S. tobaccos or the substitution of foreign tobaccos in lieu of U.S. tobaccos had been brought by them to the attention of FAS?

Mr. MENDELOWITZ. We met with the Director General of the State Enterprise for tobacco and cigarettes in Iraq, and he told us that he had received shipments under the GSM-102 Program, which he found did not meet the standards and specifications that

he thought were provided for in the contract, and he called that to the attention of the Foreign Agricultural Service.

Mr. ROSE. And when did this take place? What year did this take place?

Mr. MENDELOWITZ. I believe this was 1986.

Mr. ROSE. And did any individuals in Iraq tell you that after complaining to the appropriate U.S. supplier regarding the content of GSM tobacco that Iraq received additional tobacco as an inducement to drop the complaint?

Mr. MENDELOWITZ. Yes, we were told that. Our understanding is that an increment in volume of about 10 percent was added to the shipment as compensation for the complaint.

Mr. ROSE. Are you aware of any laws other than issues regarding false statements to Federal officials that might have been violated where additional commodities were shipped or where a GSM transaction contemplated the sale of air-conditioners or tires in addition to the contract for commodities?

Mr. MENDELOWITZ. I want to be very careful on how I answer this question because my understanding is that there is a range of issues that are currently under investigation.

Mr. ROSE. OK.

Mr. MENDELOWITZ. I would say as a general proposition, if a U.S. businessman makes a payment to a foreign government official for reasons other than permitted "grease" payments, such as to expedite Customs procedures, such activity would be prohibited by the Foreign Corrupt Practices Act.

Mr. ROSE. Did you ascertain any further information regarding the content of varied grocery store items shipped to Jordan during your overseas visit?

Mr. MENDELOWITZ. When we looked at the grocery items being shipped, we identified several items that clearly were not 100 percent U.S. contents including coffee filters, for one, that had been manufactured in Canada and a cocoa-flavored cereal that clearly came from abroad because it wasn't processed in the United States.

Basically, we found the range of commodities being shipped to the grocery store or supermarket overseas were in the same range of products that you would find in a grocery store in the United States. Much of what you find here includes imported content.

For example, canned vegetables are seasonal products in terms of growth in the United States. Some of the canned vegetables may be grown in the United States if they are canned during the right season. On the other hand, you may in a different season of the year find the canning consisting of imported horticultural products from Mexico.

While we found a handful of products that we clearly identified as foreign, there were certainly a larger number of items which had the potential for not being 100 percent U.S. products.

Mr. ROSE. I understand that the Flue-cured tobacco cooperative has been unable to participate in the Export Enhancement Program due to a decision reached by the Trade Policy Council.

In your review of the EEP program, did you come across any information with respect to this matter?

Mr. MENDELOWITZ. Our understanding is that tobacco was not a product eligible for the Export Enhancement Program.

Mr. ROSE. Is there any reason in law for that?

Mr. MENDELOWITZ. Not that I am aware of.

Mr. ROSE. What is your candid opinion regarding the management and compliance of export programs by the Foreign Agricultural Service?

Mr. MENDELOWITZ. Our current reviews indicate that there have been some positive responses on the part of Foreign Agricultural Service to implement recommendations that we have made over the past several years.

At the same time, we feel there is considerable scope for improvement that is needed to enhance the internal controls, planning, documentation of decisionmaking, and evaluation of the export programs at the Department of Agriculture.

Mr. ROSE. In a briefing that you gave our staff last night, you discussed that there might be a weakness in management that might be somehow be related to the particular structure of FAS. Would you mind elaborating on this just a little bit?

Mr. THOMAS. Yes, Mr. Chairman. What we have found in the administration of the TEA Program and GSM-102 and EEP programs is that the agricultural attaché service is heavily involved in their management. Attachés rotate between overseas and Washington assignments, and are consequently in a state of transition.

Mr. ROSE. Let me interrupt you. You mean the commercial or agricultural attachés that are stationed at our embassies around the world?

Mr. THOMAS. Yes.

Mr. ROSE. Go ahead.

Mr. THOMAS. While abroad the attachés function in an informational, analytical, and representation role. When reassigned to Washington, they often assume an export program management role.

We have found that the attaché rotation system does not lend itself to continuity of management expertise. We believe there is a need to establish more export program continuity and perhaps increase the number of nonrotational export program managers while simultaneously preserving the attaché rotational system.

When you look at the 1985 Food Security Act and the number of export programs imposed on FAS, and consider the impact of the rotation of the attachés on the management of these programs you get the sense that the rotation system to some extent disrupts the effective management of the export programs.

You need more management expertise, I think, to improve the management of these programs.

Mr. ROSE. Thank you. That is an excellent point. One last question. I understand that your staff has been looking into the bank-related aspects of Export Credit Guarantee Program transactions.

Could you tell us specifically what you have done so far and what problems you see with respect to banking institutions and to export credit guarantee programs?

Mr. MENDELOWITZ. Well, we met with several banks that participate in the GSM Program to obtain their viewpoints on the program's operation, and what we found was that the banks generally review the program as not especially profitable due to the small margins that they are allowed to capture on the interest rates.

Mr. ROSE. Not the 420 percent one, though?

Mr. MENDELOWITZ. No, nothing like that. There have not been a large number of banks participating, and what we have found is a fairly high concentration of program participation by a relatively small number of banks. One of them, as we indicated, was the Banco Nationale De La Voro, which has gotten into a major controversy reported in the press because its Atlanta branch was making literally billions of dollars of loans to Iraq without getting approval of high level officials of the bank.

Because all the risks in the program is assumed by the Federal Government, the banks may give less attention to all the fiduciary concerns that they should apply, and I think that because of that, FAS should take a close look at the rules and procedures for bank participation in the program, the desirability for having a single institution represent as much as 25 percent of the program in any 1 year, and represent, for example, all of the loans for one particular country.

There may be some benefit in increasing participation of other banks, if possible, and it spreading the risk around a little bit more.

Mr. ROSE. So, would it be fair to ask as my last question to you, then, that while FAS, because of what the OIG has done, because of what you have done, is aware of these problems, but that they are a long way from taking all the steps that in your opinion will be necessary to put this situation where it should be.

Mr. MENDELOWITZ. These are programs that involve a tremendous amount of money. If you look at the export promotion arena generally, you can begin to appreciate how substantial these funds are.

Agricultural exports represent about 10 to 12 percent of U.S. exports. Current funding on an annual basis for one program, by itself, Targeted Export Assistance Program, comes to more than the entire budget for the International Trade Administration.

That is this one program alone, TEA has more funding than the Department of Commerce gets for all its international activities. If you just look at resources the Department of Commerce has for export promotion, TEA represents four or five times the amount of money Commerce has for all its export promotion programs.

So, with respect to international trade and trade promotion, there is a lot of money involved, and the money that is involved is transferred from the public treasury to private individuals in pursuit of a public policy objective.

When this is done, I think it behooves the Department of Agriculture to have internal controls and management systems in place to assure that the program is operated according to the regulations and guidelines and rules established for the programs, and that the public policy objective is being achieved.

I think the Foreign Agricultural Service has a good way to go to put in place the kind of internal controls that would substantially reduce their vulnerability in this area.

Mr. ROSE. Thank you, and I will say this now before the questions are over, we deeply appreciate the quality and the depth of your investigation, and we know and believe that with your help, we will be able to make some substantial changes in these matters.

Thank you all very much.

Mr. BROWN. Mr. Glickman.

Mr. GLICKMAN. Thank you, Mr. Chairman. Before I ask a question, I would make a couple of comments. One, I think it is going to be necessary after this hearing clearly to bring in the Secretary of Agriculture and people responsible for the FAS now and during the time that the audits were occurring in order to get their explanation. I think we are going to have to bring in some of the exporters, and I think we are going to have to bring in some of the ag attachés from overseas to talk about this particular program because I don't think we are going to get a full view of why all of this happened.

You may have interrogated some of these folks, but we haven't, and I assume a lot of your information is based upon that. But at a minimum, the Secretary and the Department owe us an explanation of why this is going on. I assume that is going to happen.

Two, I think your point about the amount of money that goes into export programs reminds me a little bit that in the last 5 years, we have put an awful lot of money into export programs, and we may have some of the same parallels here that we had, not to HUD, but to the Department of Defense. That is, spending an awful lot of money so fast that nobody sat down and set up systems to do it well.

You are nodding your head, Mr. Mendelowitz. I wonder if you might comment on that because I know the GAO has been involved in a lot of these DOD overspending cases.

Mr. MENDELOWITZ. I think that really is an excellent observation. When funding is scarce, the agencies are very careful about how they spend it. When funding is abundant, we find that there is less care and attention to how its spent.

If you want to characterize problems at DOD in a sentence, the problems over the past 8 years have probably been associated with the fact that we threw an awful lot of money in the defense area more rapidly than we developed programs to use that money and more rapidly than we developed the oversight to make sure the money was spent well.

I think your analogy, between that and the agriculture promotion programs, is quite a good one. When we looked at TEA, one of the observations we made, when the funding was supposed to jump from $110 million to $325 million a year was that FAS didn't have either the management capability of overseeing such a substantial increase in the program, and that such a capability wasn't present in the private sector.

Businesses were not in a position to absorb and effectively use that much money.

Mr. GLICKMAN. Mr. Thomas, did you have a comment on that?

Mr. THOMAS. I think the perspective of FAS concerning the management of these programs over the past 5 years has been that they are private sector-oriented programs principally conducted through normal commercial market transactions requiring minimal government oversight.

Because of this view, FAS feels that it has no major management role and no substantial role in providing oversight. I think that is where we differ substantially with them.

Mr. GLICKMAN. Well, it has to do with the philosophy of Government which I personally don't share, and I doubt many of the people on this committee would share, and I am sure most taxpayers would be outraged and will be outraged.

Just one final question. You testified here on this program. You heard the OIG testify, and they have answered most of the specific questions, and I won't go through those again.

Do you differ with them at all in terms of any of their testimony that we should get on the record?

Mr. MENDELOWITZ. At this point, we see nothing in the OIG reports or heard nothing in the OIG answers to the questions that the committee has posed that would lead us to disagree with the information they developed or the answers they have given you.

Mr. GLICKMAN. I thank you very much, and again I support Mr. Rose's comments.

Mr. BROWN. Mr. Volkmer.

Mr. VOLKMER. I would just like to follow up a little bit on the gentleman from Kansas' questions, and approach you just a little bit differently.

I asked the OIG this question, and I think it would be probably more appropriate to ask you. When you analyze that fact that there has been what I call gross mismanagement, there haven't been guidelines, internal structures, methodologies developed to determine the value of a bonus, et cetera, in writing, so somebody can say that this was the way it was done and this is the way you do it.

All those things weren't done. That can be a problem of, like you said, of philosophy. Maybe that is where the problem was. However, I would like to know did you determine whether there was sufficient manpower to do all those things, assuming they decided that they should have been done or they would have done?

Mr. MENDELOWITZ. If you look at staffing levels at FAS over the past 8 years or so, there has been a decline from, I think, about 900 down to about 800, so that while the export promotion programs were growing in size and number and funding, the resources that the agency had to manage those programs were declining.

So, we would say that that certainly represents a problem. But, by the same token, we think there are ways of more efficiently using their available resources, and as we pointed out in our testimony, one of them would be to combine two programs like the Cooperator Market Development Program and TEA that operate quite similarly into a single program. Agriculture could more effectively use available management resources to oversee one program that combines those two objectives rather than to have two separate programs running parallel.

In fact, they are overlapping each other without a lot of coordination or cooperation between the two.

Mr. VOLKMER. In other words, they didn't even utilize the deficiencies that could have been done in the operation of the work force?

Mr. MENDELOWITZ. I think there are opportunities for efficiency.

Mr. VOLKMER. Do you see the changes taking place with FAS now as a result of recommendations by the OIG and yourself?

Mr. MENDELOWITZ. Well, I think that there are two things taking place at FAS that are worth noting. On this specific level, as I indi-

cated in my testimony, FAS has implemented a number of recommendations that we have made, and we think that shows progress.

On a more general level, I think what we have found in the past year is that there are new officials in charge of export programs in the Department of Agriculture and in the Foreign Agricultural Service that represent a substantial change in attitude with respect to being responsive to program management concerns we have surfaced over the past several years.

Mr. VOLKMER. Now, my last question has to do with the fact that OIG has stated that they were unable to get records from exporters other than the records that backed up under GSM programs. In other words, they give them invoices to show that they fulfill a shipment, but nothing to back that up, no audit trail or anything else to go into prior shipments of purchases, et cetera, to make sure that this was American-grown grain or whatever.

OIG says under proper auditing procedures it is necessary in order to do that. Do you agree with that as necessary to be able to audit and go back and looking at not only these certificates or invoices that a person hands you that fulfill this shipment, but all that was done in the past year or year-and-a-half to determine whether or not that grain, actually shown by the invoices, was going in the shipment?

Mr. MENDELOWITZ. I think the problem raised by OIG is a significant problem. As they pointed out, and I would tend to agree, you can't, in effect, follow the string to the end of the audit trail unless you have access to that information.

Mr. VOLKMER. Thank you very much. Thank you, Mr. Chairman.

Mr. BROWN. Mr. Olin.

Mr. OLIN. Thank you, Mr. Chairman. I would like to commend the GAO for putting out this very good summary report. I wanted to ask you whether over the last several years you have prepared any formal audit reports on these three export programs that might be available to the committee?

Mr. MENDELOWITZ. We have issued earlier reports in 1987 and 1988 dealing with these programs, one in 1988 on the GSM-102/103 program, a second one in 1988 on the TEA Program, a third one in 1987 on the Export Enhancement Program, and then a fourth one back in 1987 on the Cooperator Foreign Market Development Program, which I am mentioning simply because that program was tied up in a proposal we made today with respect to how to improve management over at FAS.

Mr. OLIN. Mr. Chairman, does the committee have these audit reports?

Mr. BROWN. I presume that they do. If they don't, we will make sure that they get them; yes.

Mr. OLIN. I would like to be sure the committee has these in our files.

Did the GAO conduct any audits in the same time period that the OIG was making their audit reports?

Mr. MENDELOWITZ. We have been working—or to use an agricultural metaphor—toiling in the same vineyards for the past couple of years, and we have worked carefully at coordinating what we do so that (1), we don't step on each other's toes and get under foot,

and (2), to make sure that we didn't do things that were excessively redundant.

So, yes, we have been working on the same issues, and I think we have done a pretty good job of working together to serve congressional interest.

Mr. OLIN. You tried not to duplicate the activity, obviously, but you have made comments on almost all the same points that they brought up. You have used their data where it was appropriate?

Mr. MENDELOWITZ. I think it went both ways. We have used their data when appropriate, and they used ours when it was appropriate.

Mr. OLIN. Could I ask you another question that is similar to the question that Mr. Rose was talking about on Iraq? We are trying to get into this a little deeper.

I understand that you said that in 1986, Iraq brought to the attention of the FAS a shipment that was not up to standard. Was that shipment then determined to have been a mixed shipment?

Mr. MENDELOWITZ. The Director General of the State Enterprise for Tobacco and Cigarettes believed that that tobacco shipment included foreign tobacco, and in its communications with FAS specifically raised the concern that the shipment was in fact not 100 percent U.S. tobacco.

Mr. OLIN. Could you do that last sentence over again? I didn't quite hear it.

Mr. MENDELOWITZ. In the Director General's communication with FAS, he specifically raised the concern that the shipment of tobacco was not 100 percent U.S. tobacco.

Mr. OLIN. So, to your knowledge, did the FAS ever verify whether it was mixed or not mixed?

Mr. MENDELOWITZ. My understanding is that the General Sales Manager at the time replied back to the Director General that that was a difficult problem to control, and if I remember correctly, and you are asking me to go back a ways in some of the work we did, there were inquiries made, and the whole issue was handled without any documentation. A few phone calls were made, and that is the situation as I remember it. There was nothing in FAS' files to indicate that they did much on it.

My assumption is that the subsequent work of OIG, which identified individual shipments of foreign tobacco, developed the information that would be necessary to address this specifically.

Mr. OLIN. You will have a record of who you talked with on this subject?

Mr. MENDELOWITZ. Yes.

Mr. OLIN. OK, I didn't quite understand the statements that were made with regard to the compensation that was finally offered to settle this question. Could you repeat that?

Mr. MENDELOWITZ. The Director General withdrew the complaint subsequent to negotiations with the U.S. exporter on compensation for the fact that the shipment did not meet specifications. The compensation, we were told, consisted of increasing the volume of tobacco provided for the amount paid by 10 percent.

Mr. OLIN. And this was paid by the exporter?

Mr. MENDELOWITZ. That is right. The exporter added another 10 percent in volume to the shipment.

Mr. OLIN. There is no U.S. Government contribution toward that?

Mr. MENDELOWITZ. My understanding was there was none.

Mr. OLIN. Thank you very much. Thank you, Mr. Chairman.

Mr. BROWN. Mr. Mendelowitz, I just wanted to briefly explore this recommendation that you made about combining the TEA and the Cooperator Program in an effort to improve the management.

Did you make that recommendation to the Department?

Mr. MENDELOWITZ. We actually briefed the Department recently on the progress of our work. We raised the possibility of combining the two programs, and I think that the best way to characterize their response was that it was not negative at first blush. It was something, I think, they said they would be willing to think about. That is correct.

Mr. BROWN. Well, what I am interested in is getting the pros and cons of this. You have laid out the pros pretty well. I assume the Department, after they thought about it, will respond to your recommendations with their reasons either why it should or should not be done.

Mr. MENDELOWITZ. Correct.

Mr. BROWN. And in the event that that occurs, I would like to have you provide that to the committee or send it to my office, if you would.

Mr. MENDELOWITZ. Certainly.

Mr. BROWN. This is something that we might want to take up early next year as part of our redoing the farm bill, and it would be useful to have that in the record.

Mr. Rose, do you have an additional question?

Mr. ROSE. Just one last question. I am sitting here thinking about what Mr. Nagle asked you, and I would ask you another off-the-wall question.

Has it ever occurred to any of you that the pattern of these GSM tobacco sales might have had anything to do with anything Mr. Ollie North was involved in?

By that, I mean countries that were involved with hostages? Have you ever thought about that?

Mr. MENDELOWITZ. I will be quite honest. The countries that were directly involved in the hostage issue, one of which was Iran, obviously are not eligible for receipt of commodities under any of our programs. The issue didn't come up, and quite honestly, I don't think we have thought of that as a possibility.

Mr. ROSE. Thank you.

Mr. BROWN. He would like to have you respond that some of that extra money went to support the Contras, but I am sure you did not check into that.

Thank you very much, Mr. Mendelowitz. You and all of your colleagues have been extremely helpful to us, and we appreciate it. If we have any additional questions, we will address them to you in writing.

Mr. MENDELOWITZ. Thank you, Mr. Chairman.

Mr. BROWN. That concludes this hearing for this morning.

[Whereupon, at 12:10 p.m., the hearing was adjourned, subject to the call of the chair.]

[Material submitted for inclusion in the record follows:]

UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL

STATEMENT OF JAMES R. EBBITT
ASSISTANT INSPECTOR GENERAL FOR AUDIT
OFFICE OF INSPECTOR GENERAL
U.S. DEPARTMENT OF AGRICULTURE

BEFORE A JOINT HEARING OF
THE HOUSE AGRICULTURAL SUBCOMMITTEES ON
DEPARTMENT OPERATIONS, RESEARCH AND FOREIGN AGRICULTURE;
TOBACCO AND PEANUTS;
AND WHEAT, SOYBEANS AND FEEDGRAINS

ON THE

FOREIGN AGRICULTURAL SERVICE'S ADMNISTRATION OF CERTAIN ASPECTS
OF THE GSM 102 AND 103 EXPORT CREDIT SALES PROGRAM,
EXPORT ENHANCEMENT PROGRAM, AND TARGETED EXPORT ASSISTANCE PROGRAM

NOVEMBER 16, 1989

THANK YOU CHAIRMEN BROWN, ROSE AND GLICKMAN, RANKING MINORITY MEMBERS AND MEMBERS OF THE SUBCOMMITTEES. I AM JAMES R. EBBITT, THE ASSISTANT INSPECTOR GENERAL FOR AUDIT, AND WITH ME THIS MORNING ARE CRAIG BEAUCHAMP, ASSISTANT INSPECTOR GENERAL FOR INVESTIGATIONS AND RICHARD LONG, THE DEPUTY ASSISTANT INSPECTOR GENERAL FOR AUDIT. WE ARE PLEASED TO APPEAR BEFORE YOU TODAY TO DISCUSS OUR AUDITS OF CERTAIN ASPECTS OF THE FOREIGN AGRICULTURAL SERVICE'S (FAS'S) ADMINISTRATION OF THREE MARKET DEVELOPMENT PROGRAMS: EXPORT CREDIT GUARANTEE PROGRAMS (GSM 102/103); THE EXPORT ENHANCEMENT PROGRAM; AND THE TARGETED EXPORT ASSISTANCE PROGRAM (TEA). I AM SUBMITTING MY PREPARED STATEMENT FOR THE RECORD, AND I HAVE SELECTED HIGHLIGHTS OF THAT STATEMENT TO PRESENT TO YOU.

WE ISSUED OUR AUDIT REPORTS ON THE GSM 102/103 AND EXPORT ENHANCEMENT PROGRAMS IN SEPTEMBER, 1989, AND ON THE TEA PROGRAM IN MARCH 1988. I WOULD FIRST LIKE TO DISCUSS OUR AUDIT OF THE GSM PROGRAM, FOLLOWED BY THE EXPORT ENHANCEMENT PROGRAM AND TARGETED EXPORT ASSISTANCE PROGRAM.

GSM 102/103 PROGRAM

ON OCTOBER 6, 1988, AND ON MARCH 1 AND JUNE 14, 1989, WE TESTIFIED BEFORE CHAIRMAN ROSE'S SUBCOMMITTEE REGARDING OUR AUDIT AND INVESTIGATION ACTIVITIES RELATING TO THE GSM PROGRAM. AT THOSE HEARINGS, WE STATED THAT COMMODITIES OF FOREIGN ORIGIN WERE BEING COMBINED WITH U.S. COMMODITIES AND EXPORTED UNDER THE GSM 102/103 PROGRAM. OUR ANALYSIS OF EXPORTS WITH GUARANTEES SHOWED THAT TOBACCO WAS THE PRODUCT MOST OFTEN COMBINED. HOWEVER, WE HAVE SUBSEQUENTLY FOUND THAT FOREIGN-ORIGIN VEGETABLE SEEDS, BEEF CATTLE, SOFT DRINK CONCENTRATE INGREDIENTS, AND WOOD PULP WERE INCLUDED IN EXPORTS UNDER THE GSM 102/103 PROGRAM. THESE CONDITIONS ARE DISCUSSED IN AN AUDIT REPORT WE ISSUED IN SEPTEMBER 1989.

IN FISCAL YEAR 1988, FAS ISSUED ABOUT $5.3 BILLION IN GUARANTEES FOR 64 COMMODITY GROUPS. WE ANALYZED ALL THE COMMODITIES TO DETERMINE THOSE THAT HAD THE GREATEST POTENTIAL TO INCLUDE FOREIGN CONTENT UNDER THE EXPORT PROGRAM. WE CONSIDERED FACTORS SUCH AS DIFFERENCES BETWEEN FOREIGN AND DOMESTIC COMMODITY COSTS, QUANTITIES IMPORTED, AND QUANTITIES EXPORTED. WE SELECTED 11 OF THOSE 64 COMMODITY GROUPS WITH A GUARANTEED VALUE OF ABOUT $1.1 BILLION FOR REVIEW. OF THE $1.1 BILLION, WE SAMPLED $500 MILLION IN GUARANTEED EXPORT SALES AND FOUND THAT $169 MILLION CONTAINED FOREIGN COMMODITIES. FAS HAS TAKEN SEVERAL ACTIONS IN RESPONSE TO OUR AUDIT, INCLUDING: (1) REQUIRING EXPORTERS TO CERTIFY THAT ALL EXPORTED COMMODITIES WERE 100-PERCENT U.S. ORIGIN; (2) CLARIFYING NON-AGRICULTURAL CONTENT CRITERIA; (3) COORDINATING PROGRAM ADMINISTRATION AMONG ITS DIVISIONS; (4) SPOTCHECKING EXPORTERS' RECORDS; AND (5) SUSPENDING AND DEBARRING PROGRAM VIOLATORS.

OUR INVESTIGATION OF COMPANIES ALLEGEDLY INCLUDING FOREIGN TOBACCO IN SHIPMENTS FOR WHICH THEY OBTAINED A GUARANTEE IS CONTINUING IN COORDINATION WITH THE U.S. ATTORNEY'S OFFICE IN RALEIGH, NORTH CAROLINA.

IN ADDITION TO THE FOREIGN CONTENT ISSUE, OUR AUDIT ALSO IDENTIFIED SEVERAL ISSUES REQUIRING CORRECTIVE ACTION. FIRST, WE RECOMMENDED THAT FAS PROMOTE LEGISLATION TO PREVENT EXPORTERS FROM USING COMMODITIES EXPORTED UNDER GSM, OR ANY OTHER USDA EXPORT PROGRAM, TO OBTAIN DRAWBACKS. A DRAWBACK IS THE METHOD BY WHICH IMPORTERS/EXPORTERS CAN RECOVER IMPORT DUTIES PAID TO U.S. CUSTOMS SERVICE ON IMPORTED COMMODITIES. THESE DUTIES ARE SUBSEQUENTLY REFUNDED WHEN THE IMPORTER/EXPORTER EXPORTS THE SAME TYPE OF COMMODITY. EXPORTERS IN THE GSM PROGRAM CAN USE THE U.S. COMMODITIES THEY EXPORT AS THE BASIS FOR RECOVERING DUTIES THEY PAY ON THE SAME TYPE COMMODITIES THEY IMPORT. THOSE FOREIGN COMMODITIES THEN HAVE A LOWER COST AND CAN THEREFORE MORE EASILY

DISPLACE U.S. COMMODITIES IN OUR DOMESTIC MARKETS. WE IDENTIFIED ONE EXPORTER WHO HAS APPLIED FOR DRAWBACKS OF $2 MILLION BASED UPON EXPORTS MADE UNDER THE GSM PROGRAM.

WE ALSO CITED DEFICIENCIES IN THE EXPORTERS' RECORDS. MOST EXPORTERS DID NOT MAINTAIN RECORDS TO SHOW THAT THE COMMODITY WAS OF U.S. ORIGIN OR THAT A SUFFICIENT QUANTITY OF U.S.-ORIGIN COMMODITIES WERE PURCHASED FOR EXPORT. EVERY EXPORTER DENIED US ACCESS TO THEIR NON-GSM RECORDS. WITHOUT ACCESS TO ALL RECORDS, WE COULD NOT DETERMINE THAT A SUFFICIENT QUANTITY OF U.S. ORIGIN COMMODITIES WERE AVAILABLE IN THE EXPORTER'S INVENTORIES AT THE TIME OF THE GSM SALE. ALSO, WE COULD NOT DETERMINE IF EXPORTERS WERE USING GSM PROGRAM FINANCING AS A MEANS TO GENERATE EXCESSIVE PROFIT MARGINS, AS COMPARED TO THEIR NON-GSM SALES. WE WERE ABLE TO ESTIMATE GROSS PROFIT MARGINS, EXCLUDING OVERHEAD AND OTHER INDIRECT COSTS, ON SOME GSM SALES AND FOUND SOME WHICH APPEARED EXCESSIVE. FOR EXAMPLE, AN EXPORTER OF SOYOIL REALIZED A 77.4 PERCENT GROSS PROFIT ON ITS GSM SALES. PREVENTION OF EXCESSIVE PROFITS IS IMPORTANT BECAUSE THE U.S. GOVERNMENT HAS GUARANTEED THE FINANCING OF THE CREDIT SALE AMOUNT, INCLUDING THE PROFIT. THEREFORE, IF THE BUYER DEFAULTS, THE U.S. GOVERNMENT WILL BE PAYING THESE EXCESSIVE PROFITS.

FAS HAS TAKEN ACTION TO REINFORCE RECORDKEEPING REQUIREMENTS FOR FAS EXPORTERS. HOWEVER, FAS DOES NOT BELIEVE IT IS NECESSARY FOR GOVERNMENT REPRESENTATIVES TO HAVE ACCESS TO RECORDS FOR NON-GSM TRANSACTIONS BECAUSE IT BELIEVES THERE ARE OTHER METHODS TO ACCOMPLISH THE SAME OBJECTIVE. WE CONTINUE TO BELIEVE THAT ACCESS TO EXPORTERS' NON-GSM RECORDS IS NECESSARY TO VERIFY INVENTORIES AND MONITOR PROFITS.

WE QUESTIONED THE APPROPRIATENESS OF USING THE GSM PROGRAM TO SELL COMMODITIES TO AN EXPORTER'S LICENSED OR FRANCHISED BUYERS. THESE BUYERS MUST PURCHASE

A BRAND-NAME OR TRADE MARK PRODUCT FROM A U.S. COMPANY. THEREFORE, THE GSM PROGRAM ONLY SERVES TO GUARANTEE THE FINANCING FOR SALES TO FOREIGN BUYERS WHO, BY LICENSING AGREEMENT, ALREADY MUST BUY FROM THE U.S. COMPANY. THE DEPARTMENT'S OFFICE OF GENERAL COUNSEL ISSUED AN OPINION WHICH ADVISED THAT LICENSEE/FRANCHISEE SALES ARE NOT PROHIBITED, BUT RATHER A POLICY DECISION BY FAS.

FAS HAS AGREED, WHEN CONSIDERING SPECIFIC COUNTRY PROPOSALS, TO INVESTIGATE KNOWN FRANCHISED/LICENSED BUYER SITUATIONS. FAS WILL MAKE A DETERMINATION AS TO WHETHER THE COVERAGE IS NECESSARY TO MAINTAIN OR EXPAND THE MARKET. THIS DETERMINATION WILL BE FORWARDED TO THE GENERAL SALES MANAGER.

EXPORT ENHANCEMENT PROGRAM

WE RECENTLY ISSUED AN AUDIT REPORT OF THE EXPORT ENHANCEMENT PROGRAM (EEP)[1] THE EEP WAS ESTABLISHED IN 1985 TO ENABLE U.S. EXPORTERS TO MEET PREVAILING WORLD PRICES FOR TARGETED COMMODITIES AND COUNTRIES. THE CCC PROVIDES FUNDING, CALLED BONUSES, WHICH WHEN FACTORED IN WITH THE EXPORTER'S SALES PRICES, MAKES THEIR COMMODITIES COMPETITIVE WITH THE PREVAILING WORLD PRICE. THE PROGRAM IS INTENDED TO ASSIST EXPORTERS IN COMPETING WITH SUBSIDIZING COUNTRIES, INCLUDING THE EUROPEAN COMMUNITY, (THE EC-12). OUR REVIEW CONCENTRATED ON WHEAT, BECAUSE IT COMPRISED OVER 67 PERCENT OF THE BONUSES PAID, AND ON DAIRY CATTLE, BECAUSE OF THE HIGH PER-HEAD BONUS.

AT THE TIME WE COMPLETED OUR REVIEW, FAS HAD ISSUED ABOUT $2.2 BILLION IN BONUSES BUT HAD NOT PERFORMED A PROGRAM ANALYSIS OF THE EEP TO DETERMINE IF PROGRAM OBJECTIVES WERE BEING MET AND THE PROGRAM COSTS WERE REASONABLE. SINCE OUR REVIEW, TWO STUDIES HAVE BEEN PERFORMED WITHIN USDA. THESE STUDIES ATTRIBUTED 20 TO 30 PERCENT OF THE U.S.'S EXPANDED WHEAT EXPORTS TO THE EEP.

EFFECTS OF TARGETING

FAS HAD NOT DEVELOPED WRITTEN CRITERIA FOR PARTICIPATION IN EEP. THEREFORE, WE COULD NOT EVALUATE FAS'S BASIS FOR INCLUDING INDIVIDUAL COUNTRIES IN EEP, THE POTENTIAL IMPACT ON OTHER U.S. MARKETS, OR FAS'S RESPONSE TO MARKET CHANGES THAT OCCURRED BECAUSE OF TARGETING. GENERALLY, COUNTRIES NOT TARGETED FOR EEP REDUCED THEIR PURCHASES FROM THE U.S. FAS SUBSEQUENTLY HAD TO TARGET THOSE COUNTRIES TO REGAIN LOST MARKET SHARES.

A LOOK AT SOME OF THE TARGETED COUNTRIES CAN BEST ILLUSTRATE THIS POINT. FOR EXAMPLE, THE EC-12 HAD A COMPETITIVE MARKET SHARE IN BOTH THE SOVIET UNION AND BRAZIL, BUT NEITHER WERE INITIALLY TARGETED FOR EEP. ALTHOUGH THE U.S. HAD ABOUT 30 PERCENT OF THE SOVIET UNION'S WHEAT MARKET IN 1984, THAT MARKET SHARE STEADILY DECLINED TO ZERO IN 1986. THE SOVIET UNION WAS LATER APPROVED FOR EEP IN 1987. IN BRAZIL, THE U.S. HAD 60 PERCENT OF ITS WHEAT MARKET IN 1985, HOWEVER, THAT SHARE STEADILY DECLINED TO ABOUT 5 PERCENT IN 1987, AT WHICH TIME BRAZIL WAS APPROVED FOR EEP.

CONVERSELY, FAS TARGETED COUNTRIES IN WHICH THE EC-12 WAS NOT A COMPETITIVE FACTOR. FOR EXAMPLE, FAS TARGETED EGYPT FOR EEP IN 1985, AT WHICH TIME THE U.S. HAD 30 PERCENT OF ITS WHEAT MARKET AND THE EC-12 HAD NO PORTION OF THAT MARKET. SIMILARLY, THE EC-12 WAS NEVER A COMPETITIVE FACTOR IN THE PEOPLES REPUBLIC OF CHINA. THE U.S. STILL LOST ITS' MARKET SHARE BECAUSE CHINA WAS NOT TARGETED. FAS SUBSEQUENTLY TARGETED THAT COUNTRY FOR EEP TO REGAIN OUR MARKET SHARE.

THE U.S.'S COMPETITION

EXAMPLES OF TARGETED MARKETS SUCH AS THESE SUGGEST THAT A MAIN OBJECTIVE OF EEP, THE COUNTERING OF EC-12 MARKET SHARES, MAY NOT HAVE BEEN ACHIEVED.

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SPECIFICALLY, THE WORLD WHEAT MARKET HISTORY SHOWS THAT THE EC-12'S SHARE HAS BEEN CONSTANT, EVEN AFTER FAS IMPLEMENTED THE EEP.

WE HAVE RECOMMENDED THAT FAS PREPARE AN ANALYSIS WHICH ADDRESSES COMMODITY AND COUNTRY TARGETING ACTIVITIES, THE RELATIONSHIP OF U.S. EXPORTS TO THOSE OF OTHER COUNTRIES, OVERALL COSTS FOR INCREASED MARKET SHARES, AND THE EFFECTS OF REDUCED ENDING STOCKS ON FUTURE PROGRAM ACTIVITY AND COMMODITY EXPORTS.

FAS HAS ADVISED US THAT A FINAL STUDY HAS BEEN COMPLETED WHICH ADDRESSES THESE AREAS. ALSO, FAS HAS AGREED TO ESTABLISH WRITTEN POLICIES AND PROCEDURES FOR ALL ASPECTS OF THE PROGRAM, INCLUDING CRITERIA FOR TARGETING SPECIFIC COUNTRIES.

BONUS AMOUNTS INCLUDE FREIGHT ASSISTANCE

THE EEP BONUS AMOUNTS ARE CALCULATED USING THE DELIVERED PRICE OF THE COMMODITY. AS A RESULT, THE DIFFERENCE IN COSTS BETWEEN SHIPPING FROM U.S. PORTS AND EC-12 PORTS BEING WAS IN THE BONUS CALCULATIONS. THE REASON FAS DID THIS WAS TO REDUCE THE LOCATIONAL DISADVANTAGE THE U.S. HAD IN SOME FOREIGN MARKETS. FAS ALSO MADE REDUCTIONS IN BONUS CALCULATIONS WHEN THE U.S. HAD A LOCATIONAL ADVANTAGE. WE ESTIMATE THAT THE NET EFFECT OF THESE ADJUSTMENTS WAS A COST OF $151 MILLION TO EEP FOR SIX GRAIN PRODUCTS DURING THE PERIOD SEPTEMBER 1986 THROUGH AUGUST 1988.

WE QUESTIONED THESE COSTS FOR MOST COMMODITY SALES UNDER EEP BECAUSE IT IS NOT CLEAR THAT THE FOOD SECURITY ACT OF 1985 PROVIDED FOR THE PAYMENT OF ADDITIONAL SHIPPING COSTS TO OFFSET LOCATIONAL DISADVANTAGES. RATHER, THE ACT ONLY SPECIFICALLY AUTHORIZES PAYMENT OF SHIPPING COSTS FOR EXPORT SALES OF BREEDING ANIMALS.

WE HAVE RECOMMENDED TO FAS THAT THEY OBTAIN AN INTERPRETATION FROM THE DEPARTMENT'S OFFICE OF GENERAL COUNSEL AS TO WHETHER THE ACT ALLOWS FOR PAYMENT OF SHIPPING COSTS FOR ALL PROGRAM COMMODITIES. FAS BELIEVES THAT A SUBSIDY CAN INCLUDE THE HIGHER COSTS OF SHIPPING FROM THE U.S. IN ORDER TO MAKE U.S. COMMODITIES MORE COMPETITIVE WITH THOSE OF THE EC-12 IN A TARGETED COUNTRY. FAS HAS AGREED TO OBTAIN A LEGAL INTERPRETATION ON WHETHER BONUS VALUES CAN INCLUDE FREIGHT COSTS.

BONUS VALUE CALCULATIONS

WE REVIEWED FAS'S PROCEDURE FOR DETERMINING THE EC-12 PRICE FOR WHEAT, ADJUSTMENTS IT MAKES TO U.S. WHEAT PRICES, AND THE RESULTING BONUS VALUE DETERMINATION. FAS DID NOT HAVE WRITTEN PROCEDURES FOR, NOR SUFFICIENT DOCUMENTATION TO SUPPORT, THESE CALCULATIONS. THEREFORE, WE WERE UNABLE TO DETERMINE HOW FAS ARRIVED AT ITS WORLD PRICE FIGURES. BASED UPON AVAILABLE DATA, WE BELIEVE THAT FAS'S CALCULATIONS COULD HAVE OVERSTATED THE BONUS VALUE BY UP TO $2 PER METRIC TON. IF ALL EEP SALES WERE AWARDED AT THE FULL BONUS VALUE, WE ESTIMATE THE CUMULATIVE BONUS OVERSTATEMENT AS OF AUGUST 1988 TO BE ABOUT $89.8 MILLION. HOWEVER, WE DID NOTE THAT SOME BONUS AWARDS WERE MADE AT LESS THAN THE MAXIMUM AMOUNT ALLOWABLE.

WE ALSO NOTED THAT FAS MADE ADJUSTMENTS TO THE BONUS CALCULATIONS FOR INCIDENTAL COSTS, SUCH AS POTENTIAL CLAIMS AND INTEREST COSTS. OUR REVIEW OF EXPORTERS' RECORDS SHOWED THAT, IN MOST CASES, THE ACTUAL COSTS WERE LESS THAN THE AMOUNT ALLOWED BY FAS; IN SOME CASES BY AS MUCH AS $3.07 PER METRIC TON. THE LARGEST DIFFERENCES WERE FOR SHIPMENTS TO THE PEOPLES REPUBLIC OF CHINA. HERE, FAS FACTORED IN A COST PRIMARILY FOR TREATING WHEAT FOR SNOW MOLD, EVEN IF THE WHEAT WAS SHIPPED FROM AN AREA WHERE SNOW MOLD WAS NOT A PROBLEM. OVERALL, WE ESTIMATE THAT ABOUT $25 MILLION WAS OVERPAID IN EEP BONUSES FOR

EXCESSIVE INCIDENTAL COSTS.

WE HAVE RECOMMENDED, AND FAS HAS AGREED, THAT WRITTEN POLICIES AND PROCEDURES BE DEVELOPED, AND THAT FAS DOCUMENT ANY ADJUSTMENTS IT MAKES TO PRICE QUOTES.

EXPORTERS' RECORDS

AS WITH EXPORTERS IN THE GSM PROGRAM, WE WERE UNABLE TO FULLY ASSESS THE IMPACT OF THE EEP ON EXPORTERS' OPERATIONS. IN MOST CASES, WE COULD NOT DETERMINE AN ACCURATE PROFIT MARGIN ON EEP SALES FOR TWO MAIN REASONS: 1) PROFIT AND LOSS DATA WAS MAINTAINED BY PRODUCT LINE RATHER THAN BY INDIVIDUAL SHIPMENTS, AND 2) RECORDS PROVIDED TO US BY ONE DIVISION OF A COMPANY DID NOT REFLECT THE EXPENSES AND INCOME RECORDED BY OTHER DIVISIONS WITHIN THE COMPANY FOR SUCH THINGS AS SHIPPING AND STORAGE.

WE REVIEWED 50 BONUSES RECEIVED BY THREE COMPANIES FOR WHEAT AND WHEAT FLOUR SHIPMENTS. NINETEEN OF THESE 50 TRANSACTIONS RECORDED NEGATIVE MARGINS AS LOW AS 18.5 PERCENT. THESE 19 WERE ALL WHEAT SALES. OTHER WHEAT SALES SHOWED PROFIT MARGINS OF UP TO 14.8 PERCENT. THE LARGEST PROFITS WERE ON WHEAT FLOUR, WHERE WE FOUND MARGINS OF UP TO 33 PERCENT. WE COULD NOT DETERMINE THE TRUE PROFIT MARGINS BECAUSE THESE PERCENTAGES DID NOT INCLUDE OVERHEAD AND OTHER INCIDENTAL COSTS.

IN CERTAIN INSTANCES, WE WERE ABLE TO COMPARE EXPORTERS' ESTIMATED COST FIGURES FAS USED IN ITS BONUS CALCULATIONS WITH THE EXPORTERS' ACTUAL COSTS. FOR EXAMPLE, AN EXPORTER OF WHEAT FLOUR OBTAINED TWO AGREEMENTS, EACH TO EXPORT 15,000 METRIC TONS. THE EXPORTER ESTIMATED A SHIPPING COST OF $28.25 AND $27.25, RESPECTIVELY, PER METRIC TON FOR THE TWO AGREEMENTS. HOWEVER, ITS RECORDS SHOWED THAT THE ACTUAL FREIGHT COST WAS $18.00 PER METRIC TON FOR BOTH AGREEMENTS. THOSE TWO AGREEMENTS ALREADY CONTAINED AN ESTIMATED GROSS MARGIN

OF ABOUT $925,000. THE LOWER ACTUAL SHIPPING COST PROVIDED AN ADDITIONAL BONUS OF $307,000.

FAS BELIEVES THAT THE BIDDING PROCESS OF THE EEP WOULD, ITSELF, RESULT IN THE LOWEST POSSIBLE BID FOR MAKING A SALE, THEREBY ELIMINATING THE CHANCE FOR EXCESSIVE PROFITS. WE AGREE THAT THE BIDDING PROCESS IS A MAJOR FACTOR IN PREVENTING SUCH ABUSE IF THERE ARE SEVERAL BIDDERS. HOWEVER, WE NOTED INSTANCES WHERE ONLY ONE EXPORTER BID ON A SALE. THEREFORE, WE RECOMMENDED TO FAS THAT IT CHANGE THE LANGUAGE IN ITS BID ANNOUNCEMENTS TO INSURE THAT EXPORTERS UNDERSTAND THAT THEY MUST MAINTAIN AND PROVIDE RECORDS THAT WILL ENABLE USDA OFFICIALS TO ANALYZE THE FINANCIAL RESULTS OF THE EXPORTER'S PARTICIPATION IN EEP.

DAIRY CATTLE

IN JUNE 1986, DAIRY CATTLE WERE SHIPPED BY BOTH AIR AND SEA TO DESTINATIONS SUCH AS EGYPT, IRAQ, AND ALGERIA. EEP BONUSES RANGED UP TO $1,800 PER HEAD. DURING THIS EARLY PERIOD, FAS DID NOT HAVE EXPERIENCE IN DETERMINING COSTS INVOLVED IN EXPORTING DAIRY CATTLE AND DID NOT ANTICIPATE SOME OF THE PROBLEMS EXPORTERS WOULD ENCOUNTER EXPORTING LIVE ANIMALS. OUR REVIEW WAS LIMITED TO INITIAL SALES AWARDED UNDER THE BIDDING PROCESS.

THE ORIGINAL EEP DAIRY CATTLE PROGRAM, WHICH USED THE BIDDING PROCESS TO AWARD SALES, WAS SUSPENDED BECAUSE OF THE HIGH COST. IN ITS PLACE, FAS IMPLEMENTED A PREANNOUNCED BONUS PROGRAM WITH STATED BONUSES OF $700 TO $900 PER HEAD, DEPENDING UPON DESTINATION. HAD THESE PREANNOUNCED BONUS AMOUNTS BEEN USED FOR THE INITIAL SALES, BONUSES PAID WOULD HAVE BEEN $18 MILLION LESS THAN THEY ACTUALLY WERE.

FAS ALSO PERMITTED SOME CATTLE SHIPMENTS TO BE MADE BY AIR RATHER THAN SEA,

BUT DID NOT HAVE CRITERIA DEVELOPED TO JUSTIFY THE MORE EXPENSIVE MODE OF TRANSPORTATION. FOR EXAMPLE, FAS APPROVED FIVE AGREEMENTS FOR EXPORTERS TO SHIP 1,825 DAIRY CATTLE BY AIR TO EGYPT AT A TOTAL BONUS OF $3,407,350. HAD THOSE CATTLE BEEN SHIPPED BY SEA, THE TOTAL BONUS WOULD HAVE BEEN ABOUT $2.6 MILLION; A SAVINGS OF $806,000.

THE HIGH BONUSES PAID MADE IT POSSIBLE FOR EXPORTERS TO ENTER INTO COSTLY FINANCIAL ARRANGEMENTS WITH PRIVATE INVESTORS AND CORPORATIONS IN ORDER TO OBTAIN OPERATING CAPITAL AND TO MEET PERFORMANCE SECURITY REQUIREMENTS. WE NOTED THAT TWO OF THE THREE EXPORTERS WE VISITED HAD TO PAY FROM 25 TO 50 PERCENT OF THEIR NET PROFITS TO INVESTORS. EACH OF THE THREE EXPORTERS HAD SUBSTANTIAL NET PROFIT MARGINS ON THEIR EXPORT SALES BEFORE PROFIT SHARING WITH INVESTORS. THESE PROFIT MARGINS RANGED FROM ABOUT 10 TO 24 PERCENT. A SPECIFIED PERCENTAGE OF THE PROFITS WAS THEN SHARED WITH THE EXPORTERS' RESPECTIVE INVESTORS. THE RATES OF RETURN TO THE INVESTORS RANGED FROM ABOUT 20 TO 50 PERCENT.

WE ALSO CITED PROBLEMS WITH FAS TIMELY RESPONDING TO EXPORTER REQUESTS FOR CONTRACT MODIFICATIONS AND APPEALS. FAS HAD NOT ESTABLISHED TIMEFRAMES FOR GRANTING EXTENSIONS, ASSESSING LIQUIDATED DAMAGES, REEXAMINING BONUS LEVELS AND IMPOSING BONUS REDUCTIONS. THIS CAUSED EXPORTERS DIFFICULTY IN THEIR OPERATIONS. FOR EXAMPLE, ONE EXPORTER SUBMITTED THREE EXTENSION REQUESTS ON THE SAME DAY. FAS DID NOT NOTIFY THE EXPORTER OF ITS APPROVAL UNTIL 77 DAYS AFTER THE REQUESTS WERE MADE.

FAS ALSO DID NOT ESTABLISH TIMEFRAMES FOR DETERMINING WHETHER TO ASSESS LIQUIDATED DAMAGES. WE NOTED THAT FAS HELD A TOTAL OF OVER $9 MILLION IN EXPORTERS' PERFORMANCE SECURITIES FOR PERIODS RANGING FROM 68 TO 349 DAYS WHILE MAKING SUCH DETERMINATIONS. SIMILAR PROBLEMS WERE FOUND WITH IMPOSING

BONUS REDUCTIONS AND RESPONDING TO EXPORTERS' APPEALS.

PRESENTLY, THE DAIRY CATTLE EXPORT PROGRAM IS NOT ACTIVE. WE HAVE MADE SEVERAL RECOMMENDATIONS TO FAS FOR THE IMPROVEMENT OF THEIR MANAGEMENT OF DAIRY CATTLE EXPORTS SHOULD THIS PROGRAM BECOME ACTIVE AGAIN. OUR RECOMMENDATIONS INCLUDED REVIEWING BONUS LEVELS PERIODICALLY TO ENSURE THEY REFLECT REALISTIC COSTS, DEVELOPING WRITTEN GUIDELINES FOR APPROVING MODE OF TRANSPORTATION, IMPROVEMENT IN SALES CONTRACT TERMS AND CONDITIONS, AND ESTABLISHING TIMEFRAMES FOR COMPLETING VARIOUS ADMINISTRATIVE ACTIONS. FAS HAS AGREED TO: (1) PERFORM PERIODIC REVIEWS OF BONUSES AND PERPARE WRITTEN GUIDELINES FOR APPROVING BONUSES, (2) ESTABLISH PROCEDURES AND TIMEFRAMES FOR THE TREATMENT OF NON-PERFORMANCE CASES AND FOR THE RE-EXAMINATION OF BONUS LEVELS AND IMPOSING BONUS REDUCTIONS; (3) SHORTEN THE RESPONSE TIME FOR EXTENSION REQUESTS; (4) REQUIRE EXPORTERS TO SUPPLY COPIES OF SIGNED SALES COMTRACTS.

TARGETED EXPORT ASSISTANCE PROGRAM

I WOULD NOW LIKE TO SUMMARIZE SOME SIGNIFICANT ISSUES FROM OUR AUDIT OF THE TARGETED EXPORT ASSISTANCE (TEA) PROGRAM, WHICH WE ISSUED IN MARCH 1988. THE TEA PROGRAM WAS ENACTED BY THE FOOD SECURITY ACT OF 1985. WE BEGAN OUR REVIEW DURING FAS'S INITIAL IMPLEMENTATION OF THE PROGRAM IN 1986. THE PURPOSE OF THE TEA PROGRAM IS TO REIMBURSE PARTICIPATING ORGANIZATIONS FOR EXPENSES INCURRED FOR CONDUCTING PROMOTIONAL ACTIVITIES IN SPECIFIC COUNTRIES TO OVERCOME THE ADVERSE EFFECTS OF UNFAIR FOREIGN TRADE PRACTICES ON ELIGIBLE AGRICULTURAL COMMODITIES OR PRODUCTS. CUMULATIVE AUTHORIZED FUNDING FOR THE 5-YEAR PERIOD ENDING SEPTEMBER 30, 1990 IS $730 MILLION, TO BE PROVIDED BY COMMODITY CREDIT CORPORATION CERTIFICATES.

A BASIC PRINCIPLE OF TEA IS THAT IT IS A JOINT EFFORT BETWEEN THE U.S. GOVERNMENT AND THE PARTICIPATING ORGANIZATIONS. SPECIFICALLY, THE PARTICIPANT IS EXPECTED TO MAKE A GOOD FAITH EFFORT TO CONTRIBUTE A PORTION OF THE RESOURCES NECESSARY TO CARRY OUT THE PROMOTION ACTIVITY. THESE CONTRIBUTIONS CAN COME FROM EITHER THE PARTICIPANT'S OWN RESOURCES OR THOSE OF THIRD PARTIES. THIRD PARTIES ARE USUALLY PRIVATE FOREIGN COMPANIES WHO WORK JOINTLY WITH THE U.S. PARTICIPANT IN MANAGING THE PROMOTION ACTIVITY IN THEIR OWN COUNTRIES.

OUR AUDIT IDENTIFIED NUMEROUS DEFICIENCIES WITH THIS FUNDING ARRANGEMENT. FOR EXAMPLE, PARTICIPANTS PROPOSED TO FAS TO SPEND UP TO SEVERAL MILLION DOLLARS, WHICH COULD INCLUDE THIRD PARTY FUNDS, IN CONJUNCTION WITH TEA FUNDS FOR A SPECIFIED PROMOTION ACTIVITY. PARTICIPANTS RECEIVED FUNDS BASED UPON AGREEMENTS WITH FAS RESULTING FROM THOSE PROPOSALS. OUR SUBSEQUENT REVIEW OF EIGHT PARTICIPANTS' RECORDS SHOWED:

- AT THE TIME OF THEIR PROPOSALS, SIX HAD NO DOCUMENTATION TO SUPPORT A TOTAL OF ABOUT $23 MILLION IN THIRD PARTY CONTRIBUTIONS WHICH THEY HAD AGREED TO PROVIDE.

- FIVE OF THESE SIX HAD NO DOCUMENTED AGREEMENTS WITH THEIR THIRD PARTY PARTICIPANTS TO PROVIDE ANY FUNDING.

- THREE PARTICIPANTS DID NOT OBTAIN AGREEMENTS WITH THEIR MEMBERS FOR ASSESSMENTS NECESSARY TO MEET $3 MILLION IN CONTRIBUTIONS THEY AGREED TO MAKE TO THE PROGRAM.

- ONE PARTICIPANT DID NOT HAVE THE FINANCIAL RESOURCES TO MAKE ITS PROPOSED $425,000 CONTRIBUTION AND MADE THAT CONTRIBUTION BY USING PREMIUMS IT RECEIVED FROM SELLING THE CCC CERTIFICATES IT SUBSEQUENTLY

RECEIVED FROM FAS.

- ONE PARTICIPANT USED MARKETING EXPENSES INCURRED BY ITS LICENSEES, WHO WERE NOT PARTICIPATING IN THE TEA PROGRAM, TO CLAIM AND RECEIVE $2.4 MILLION IN TEA REIMBURSEMENTS. AFTER WE QUESTIONED THIS PAYMENT, THE PARTICIPANT SUBSEQUENTLY REPAID THE $2.4 MILLION TO FAS.

WE ALSO FOUND DEFICIENCIES IN U.S. PARTICIPANTS' ACCOUNTING SYSTEMS, LACK OF DOCUMENTATION AND ESTABLISHED CRITERIA BY FAS TO SUPPORT THE FINAL FUNDING LEVEL.

WE HAVE MADE RECOMMENDATIONS FOR FAS TO TAKE CORRECTIVE ACTION ON ALL THESE DEFICIENCIES. EXCEPT FOR MAKING PARTICIPANT CONTRIBUTIONS MANDATORY, FAS HAS TAKEN CORRECTIVE ACTION ON ALL OUR RECOMMENDATIONS. WE ARE CONTINTUING TO WORK WITH FAS ON THIS ISSUE.

CURRENT INITIATIVES

WE ARE CURRENTLY CONDUCTING AUDIT SURVEYS OF SEVERAL FAS MANAGEMENT AND PROGRAM AREAS, INCLUDING: 1) THE FAS COMPLIANCE REVIEW STAFF, 2) THIRD PARTY CONTRIBUTIONS, 3) FOREIGN DEBT MANAGEMENT, AND 4) FOREIGN OPERATIONS AND CURRENCY USE PAYMENTS. ALSO, FOR FISCAL YEAR 1990, OIG INTENDS TO REVIEW THE MARKET DEVELOPMENT FUNCTIONS WITHIN THE AGRICULTURAL RESEARCH SERVICE AND FAS, AND THE USE OF SECTION 32 FUNDS FOR MARKET DEVELOPMENT PURPOSES.

THIS CONCLUDES MY STATEMENT, I WILL BE HAPPY TO ANSWER ANY QUESTIONS YOU MAY HAVE.

United States General Accounting Office

GAO Testimony

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Status Report on GAO's Reviews of the Targeted Export Assistance Program, the Export Enhancement Program, and the GSM-102/103 Export Credit Guarantee Programs

Statement of
Allan I. Mendelowitz, Director
Trade, Energy, and Finance Issues
National Security and International Affairs
Division

Before the Subcommittees on Department Operations, Research and Foreign Agriculture; Tobacco and Peanuts; and Wheat, Soybeans, and Feed Grains
Committee on Agriculture
House of Representatives

GAO/T-NSIAD-90-12

Messrs. Chairmen and Members of the Subcommittees:

We are pleased to be here today to discuss with you the status of our ongoing work on several programs administered by the Department of Agriculture's Foreign Agricultural Service: (1) the Targeted Export Assistance (TEA) Program,[1] (2) the Export Enhancement Program (EEP), and (3) the GSM-102/103 Export Credit Guarantee Programs. All of these programs have undoubtedly contributed to increases in U.S. agricultural exports. However we have identified numerous program management problems which need to be addressed.

THE TARGETED EXPORT ASSISTANCE PROGRAM

Our review of the TEA program, requested by Congressman Schumer, examines the extent to which FAS has implemented the recommendations made in our May 1988[2] report. The TEA program was mandated by the Food Security Act of 1985 to counter or offset the adverse effects of foreign competitors' unfair trade practices and thereby increase U.S. agricultural exports. Since the legislation did not specify how this program should be carried out, the Foreign Agricultural Service (FAS) decided to establish a market development assistance program similar to that

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[1]Attachments I through III provide more detailed information on the TEA Program.

[2]Review of Targeted Export Assistance Program (GAO/NSIAD-88-183).

of the Cooperator Market Development Program, for commodities and products adversely affected by unfair trade practices.

This program is now in its fifth and final year of funding. In each year of the program, the total authorized amount was allocated. For fiscal years 1986 through 1988, the annual allocations amounted to $110 million, and for 1989 and 1990, they amounted to $200 million. Approximately 46 not-for-profit agricultural organizations have participated in each year of the program and more than 200 for-profit private firms have received benefits under the program each year.

Unlike the Cooperator program, which in the past has focused on the export promotion of bulk commodities, the TEA program primarily focuses on the export promotion of high value products, including such horticultural commodities as fruits and nuts. Prior to TEA, commodity groups representing high value products had claimed that ongoing export programs were not adequately addressing their market development needs. The majority of promotion under TEA is designed to make consumers aware of the advantages of U.S. products and is achieved through such activities as in-store demonstrations and print and media advertising. These activities are referred to as "consumer promotion."

Over 50 percent of TEA funds for fiscal year 1989 were spent in Asian markets, with promotions in Japan alone accounting for 35 percent of TEA funds. European countries were the next largest targeted markets, with promotions in the United Kingdom accounting for over 12 percent of TEA funds. In each year of the program, the top 15 commodity organizations, ranked by amount of TEA funds received, accounted for over 60 percent of TEA funds. For fiscal year 1989, the branded portion of the TEA program, in which activities are aimed at establishing consumer loyalty to a particular brand, accounted for approximately 35 percent of the TEA allocation. The generic portion of the program, in which activities are designed to increase the total market for that commodity with no particular brand being promoted, accounted for the remainder.

Although the TEA program is modeled after the long-standing Cooperator program, there are some differences. For fiscal years 1989 and 1990, TEA funding was over five times greater than that of the Cooperator program. In addition, rather than using appropriated funds as does the Cooperator program, TEA uses generic commodity certificates issued by the Commodity Credit Corporation. While authorized expenditures under TEA were originally more restrictive than those of the Cooperator program, some restrictions, such as disallowing payment of salaries for overseas personnel, have been lifted.

Another difference is that TEA applicants are required to demonstrate the extent to which their commodities or products have been affected by unfair trade practices. Most not-for-profit agricultural organizations have been able to demonstrate impacts from one or more unfair trade practices; FAS officials told us that the requirement has caused some private firms, representing processed products, to be denied participation in the program, because they were unable to identify an unfair trade practice.

Finally, although the activities of both programs are similar, the Cooperator program is intended to achieve long-term market access while the TEA program is geared more toward achieving direct sales. FAS officials note the success of the TEA program by citing increased exports. While some level of increased exports would be expected as a result of a large infusion of resources into a targeted market, a simple increase in exports--which can be caused by a large number of other variables--is not sufficient proof of the success of the program.

Office of Inspector General Report on the Targeted Export Assistance Program (No. 07099-14-Hy)

In its March 1988 report on the TEA program, Agriculture's Office of Inspector General (OIG) focused on the TEA participants' administrative capability to manage their TEA funds and on FAS management of the program. As we testified before this Committee in July 1988, we agreed with the OIG's

recommendations that FAS provide better guidance to the participants on contracting out for services, third-party contributions, and evaluation requirements. This OIG report also expressed concern that FAS was not adequately documenting its program decisions to ensure that they were in accordance with TEA guidelines.

In our follow-up review of the TEA program, we have coordinated extensively with the OIG, since it has been reviewing FAS implementation of OIG's earlier recommendations, particularly focusing on participant and third-party contributions.

TEA Program Administration Lacks Sufficient Management Control and Accountability

In our May 1988 report on TEA, we made several recommendations relating to management control and accountability. In the follow-up review which we are now concluding, we examined the extent to which FAS has implemented our recommendations. FAS has made some improvements in program administration; however, we remain concerned that FAS does not yet have an adequate system of internal controls and is not exercising sufficient oversight of the program.

Inadequate documentation

FAS has not been sufficiently documenting program decisions. As we noted in the May 1988 report, FAS was not documenting the

funding allocation decision process to clearly show how the funding criteria were applied and prioritized and the basis for those decisions.

Our current review indicates that FAS continues to make major funding decisions based on limited written information and relies on its marketing specialists to verbally explain the suitability of the applicants and the rationale for the recommended funding amounts. The marketing specialists are primarily responsible for reviewing the applications to the TEA program and writing summaries on each application. These summaries, which average four pages in length, include a brief discussion of what the applicant proposes to do with the requested funding amount. These summaries are then forwarded, with a recommendation from the Assistant Administrator for Commodity and Marketing Programs, through the Administrator, FAS, to the Undersecretary for International Affairs and Commodity Programs for final approval. We have been told by FAS officials that these summaries are the main source of documentation for their TEA allocation decisions.

A review of all TEA summaries for funding for fiscal years 1989 and 1990 provides little insight on how FAS applies and prioritizes the criteria. We recognize that the decisions are based not only on the application criteria but also on such factors as balancing the needs of all commodity division

requests. FAS officials told us that they do not have time to fully document program decisions. We believe that such documentation is essential to ensure accountability and fairness. As currently written, the summaries do not address the importance of the various criteria to funding decisions. For example, some participants that lack prior market development experience were denied participation in the program while others with a similar lack of experience received TEA funds. Other criteria which are mentioned most often but the importance of which seems to vary depending on the applicant are (1) the administrative capability of the organization to carry out the program, (2) the amount of damage suffered from unfair trade practices, (3) the extent to which the organization represents U.S. agricultural product interests, and (4) whether the commodity or product is in adequate supply.

The TEA summaries were improved for fiscal year 1990 by incorporating, on a more consistent basis, information on evaluation results and findings from the FAS Compliance Review Office. However, not all summaries included this information and we do not know whether there were no evaluation results or findings from the Compliance Review Office or whether they were not significant enough to be included in the decisions. Since FAS officials told us that these summaries are the main source of documentation for the funding allocation decision process, we believe that sufficient information should be included to enable

an objective observer to understand how the process works and why decisions are made.

These summaries do not include information on funding received through the Cooperator program. Approximately half of the 46 not-for-profit TEA participants also receive funding through the Cooperator program and we saw little coordination between the two programs. Also, for fiscal year 1990, the TEA summaries do not include information on past allocations, approved budgets, expenses, and contribution amounts for each participant. While this information may be discussed in closed door meetings with the Assistant Administrator, we believe that it should be included in the summaries to ensure that the histories of the applicants are apparent.

Documentation is an essential part of an adequate system of internal controls. We believe that better documentation of the funding process and of other major program decisions is needed to improve accountability.

Participant contributions

We continue to be concerned that FAS is not documenting the rationale for the amount and type of participant contributions to the program. Contributions may be in the form of cash or goods and services and may come from a third party as well as from the

TEA participant. FAS officials continue to stress that contributions are not legislatively required and that a uniform standard cannot be applied to TEA participants, since their ability to contribute varies. We believe that since FAS is providing significant funding to the participants, FAS officials should explain in writing how they determine contribution amounts for each participant.

FAS officials told us that they are trying to establish a greater degree of consistency in setting contribution amounts without limiting participation; however, these rates continue to vary substantially. Several FAS officials told us that beginning with fiscal year 1989, FAS policy for the generic portion of the TEA program was that all TEA participants should contribute at least 5 percent in cash. However, there are no formal guidelines on this. In the branded portion of TEA, reimbursement rates vary among commodities. While FAS officials have said that they are attempting to establish a 50-percent reimbursement rate for all private firms promoting their own labels, some firms in practice are receiving a preferential reimbursement rate and FAS has yet to provide a suitable explanation for the disparate treatment.

TEA guidelines

During the first 3 years of the program, changes in the guidelines and updates on program operations were primarily

communicated to the TEA participants through the Planning, Review, and Operations Committee (PROC) of the U.S. Agricultural Export Development Council. We criticized FAS use of this committee in our May 1988 report because it did not include all TEA participants. The Council has since disbanded this committee and no alternative formal mechanism for communicating with participants has been established.

Agriculture's OIG, the Office of Management and Budget, and GAO concluded that FAS should change the guidelines to regulations. We believe this recommendation would be a step toward improving program administration. FAS does not agree that regulations should be established because it believes that flexibility is necessary when managing a market development program. However, establishing regulations in place of the guidelines could eliminate much of the participants' confusion and concern caused by frequent guideline changes with little notice or explanation. It could improve communication between FAS and the participants by establishing a formal process for changing procedures including an opportunity for public comment. The OIG has said that the way FAS operates the program represents an abuse of its discretionary authority. We believe that the TEA program should be operated in such a way as to ensure fairness and consistency.

FAS Efforts to Evaluate the TEA Program

Our May 1988 report pointed out that (1) FAS was not uniformly requiring participants to evaluate their activities, (2) the TEA guidelines provided no guidance on how to make evaluations, and (3) FAS was not systematically tracking and using evaluation results.

Subsequently FAS established evaluation guidelines, effective for fiscal year 1989. To indicate its commitment to evaluating market development activities, FAS has been delaying approval of participants' activity plans until those plans include an explanation of how the participants will measure the effectiveness of their activities. While the new guidelines indicate types of evaluations and who is responsible for conducting them, they are not specific enough to prevent confusion among many participants. FAS application of the evaluation guidelines does not appear to be consistent. For example, some participants must submit quarterly evaluations while others are required to submit them only once a year.

In August 1988, FAS established an evaluation branch within the Marketing Programs Division. Although this branch is over a year old, it has only recently been fully staffed, with 6 professional positions. FAS established this branch to oversee program evaluation of the TEA and Cooperator programs. While it

did establish general evaluation guidelines, this branch appears to be doing little to track and analyze evaluation results. This branch has no substantial coordinating or enforcing role with respect to the evaluation requirements, and there is no indication that it is planning to evaluate the success of the TEA program overall. The new Assistant Administrator for Commodity and Marketing Programs said that he would like to see this branch more involved in assessing evaluation results and conducting cross- commodity analyses.

FAS continues to rely too heavily on an increase in exports as proof that the TEA program is a success. It is widely accepted that several factors cause exports to increase, such as the depreciation of the dollar and reduced import barriers. Therefore, to more effectively manage the TEA program, FAS may want its evaluation branch to analyze the results of all participant evaluations and initiate an evaluation of the net results of the overall program. By continuously analyzing the impact of the TEA and Cooperator programs in the various markets, FAS may be in a better position to change program direction to reflect up-to-date market conditions.

Combine the TEA and Cooperator Programs

One way for FAS to improve the management of its market development programs could be to combine the TEA and Cooperator

programs. Combining the two programs would probably be a more efficient use of FAS resources. Marketing specialists and other FAS officials presently spend their time dealing with the two programs separately since they operate under different deadlines. Little coordination exists between the two programs. When TEA funding levels are being discussed, there is no documentation on Cooperator funding received by the applicant or on the applicant's performance in the Cooperator program. FAS officials said that their staff is so busy with day to day operational and administrative issues that they have little time for documentation. Combining the two programs, or possibly establishing a new program to replace them, may help to overcome such inherent problems.

Because the goal of combining the two programs would be to improve program administration, we believe that guidelines should be changed to regulations. As we noted earlier, this could improve communication and also, we believe, cooperation between the participants and FAS. It could serve to reduce confusion and misunderstanding among the participants and, consequently, help to prevent waste or misuse of resources. FAS officials have often told us that their Compliance Review Office will discover any instances of mismanagement. We believe that more effort should be made to prevent mismanagement from ever occurring. Requirements in a market development program should be consistent

and clear so that all participants are treated fairly and fully understand their responsibilities.

Finally, combining both programs could help prevent duplication of effort, if all activities were under one program with one set of criteria. This, coupled with other corrective action on the part of FAS concerning management oversight, would inevitably lead to a more efficiently managed and more effective program.

Before the two programs could be combined, the following issues would need to be considered:

-- The merits of using generic and/or branded promotion and the percent of total funds that should be allocated to each type.

-- The amount of emphasis to place on exports representing high value products and/or bulk commodities.

-- The priority for providing funds for new market development and/or maintaining established markets.

-- The merits of allowing large, well established private firms to participate and/or focusing resources more on helping

small, new-to-market firms establish a foothold in the market.

-- The appropriate balance in the program between compensation for unfair trade practices and market development.

-- The establishment of criteria for the amount of time that participants could remain in the program before they would be expected to maintain their market presence on their own.

THE EXPORT ENHANCEMENT PROGRAM

Our current review updates and expands upon the issues addressed in our March 1987 report,[3] and our July 31, 1989 testimony before the Subcommittee on Wheat, Soybeans, and Feed Grains. Our review is being conducted at the request of the Chairman, House Committee on Agriculture; Congressman Conte, the Ranking Minority member of the House Committee on Appropriations; and Congressman Schumer.

During the 2 years since our last report, conditions under which the EEP operates have changed considerably. The number of targeted countries has increased from 40 to 65. Total EEP sales have risen from $1.3 billion to over $8.9 billion as of

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[3]Implementation of the Agricultural Export Enhancement Program (GAO/NSIAD-87-74BR).

November 2, 1989, and the market value of EEP bonus awards has grown from $868 million to over $2.6 billion. Over $1.8 billion of the bonuses supported wheat sales, 77 percent of which were to five countries; the Soviet Union, China, Algeria, Egypt, and Morocco. The remaining EEP commodity sales have been in wheat flour, barley, barley malt, semolina, rice, vegetable oil, sorghum, frozen poultry, table eggs, poultry feed, and dairy cattle.

In the past year, the world supply of wheat has become relatively tight due to adverse weather conditions and decisions by some producing countries to reduce production. World prices for wheat have risen as a result. The U.S. government is now using EEP more selectively, and it continues to emphasize the program's importance as a trade negotiating tool.

Considering these changing conditions, Agriculture's OIG Audit Report No. 07099-18-Hy comes at a useful time. The report contains valuable insights into EEP's administration and offers recommendations for strengthening program effectiveness. Our ongoing EEP review supports, and in some cases expands upon, issues raised in the OIG report.

EEP's Impact on Increasing U.S. Agricultural Exports

In the last several years, U.S. agricultural exports have increased significantly. However, as we previously reported it is difficult to determine exactly how much of these increases were due to EEP. EEP's effect cannot be easily isolated from that of other policy and economic variables which have contributed to increased agricultural exports--lower loan rates, availability of export financing and other U.S. government assistance, depreciation of the U.S. dollar against major competitor currencies, production shortfalls, and other changes in global economic conditions. Recent studies estimate that U.S. agricultural exports have increased due to EEP, but they differ on the magnitude. The additionality estimates range from 2 to 30 percent and are greatly influenced by the assumptions made and the time period covered.

Furthermore, the fact that the EEP is "targeted" adds more complications in determining its effect. While exports may increase in the targeted markets, the overall effect on U.S. exports worldwide is uncertain. Competing suppliers may respond by displacing potential U.S. sales in uhtargeted markets. In addition, as the OIG concluded, non-targeted countries may have reduced their U.S. purchases, thereby creating the need to target those countries to regain lost market shares.

EEP does appear to have been critical to making sales in certain markets, such as wheat sales to the Soviet Union and China. During periods of surplus supplies on the world market, these importing countries took advantage of competition among exporters to obtain the best possible price and terms. Without EEP to make U.S. exports competitively priced, it is highly unlikely that these sales would have taken place. In addition, officials in Algeria, Egypt, Jordan, and Iraq told us that EEP was essential to enable U.S. exporters to make sales because these countries are "price buyers" (i.e. they buy at the best price available regardless of the source). They also noted that many EEP sales depended on the availability of U.S. export credit guarantees.

Changes in EEP Targeting Strategies

The EEP was designed to be targeted and discretionary rather than an across-the-board program. Proposals for EEP subsidies were to "target a specific market to challenge only the competitors who overtly subsidize their exports," namely the European Community (EC). Originally, the EEP's primary targets were countries that made significant purchases of subsidized EC exports. However, over time the program expanded to include countries that had a small EC market presence and then to countries where the EC was only contemplating a presence. As the EEP displaced the EC in one market, the EC turned to another

country's market, making that country eligible for EEP benefits as well. The EEP grew to 65 targeted countries in 4 years.

Perhaps the most controversial aspects of the EEP targeting strategy were the administration's decisions regarding the Soviet Union. That country was initially excluded from the program despite the fact that the EC's share of the Soviet wheat market rose from 5 to 22 percent from the 1981 to the 1985 crop year. Agriculture initially claimed that the Soviet Union was excluded because the non-subsidizing competitors had about a 48-percent share of the market in crop year 1985. Non-subsidizers, however, had equal or greater shares of other markets targeted under the EEP, such as Egypt, Iraq, Jordan, and Sri Lanka. The Soviet Union had been excluded from the program until August 1, 1986, for foreign policy reasons. It was then made eligible for EEP sales and has since become the largest importer under the program.

Impact of EEP on Competitors

The OIG found that while the EC's wheat market shares have generally increased since the EEP's inception, those of Australia, Argentina, and Canada have decreased. While the OIG noted that the decreased market shares could be the result of lower wheat supplies, it cautioned that the continuation of EEP could adversely affect these countries' exports should their

production increase. The OIG's analysis showed an inverse relationship between the U.S. wheat market share and total market shares held by these three countries. More importantly, changes in the U.S. market share appear to have relatively little effect on the EC market share. OIG thus questioned EEP's ability to challenge EC export markets without harming other competitors.

Australian and Canadian officials told us that their countries have been adversely affected by EEP, both in terms of lower prices for their commodities and reduced market shares.

Australia

Australia has been most vocal in its opposition to the EEP, stating that EEP has adversely affected its wheat exports. While Australian government and farm industry representatives and U.S. Agriculture officials agree that EEP contributed to the depression of world wheat prices between 1985 and 1988 and, consequently, to the reduction in Australian wheat export earnings, there is no consensus on the extent of EEP's effect.

According to a recently released Australian study,[4] the EEP has cost Australian wheat growers between $150 million and $238 million, due to reduced average prices on wheat exports and a

[4]U.S. Grain Policies and the World Market, Policy Monograph No. 4, Australian Bureau of Agricultural and Resource Economics, released in October 1989.

consequential decline in wheat production. The study points out that in 1987 the estimated cost to the Australian wheat industry was far greater than to the EC's, because exports to EEP-targeted markets constituted a far larger proportion of Australia's total production.

Australian officials told us that the decline in export prices encouraged producers to move out of wheat production; plantings fell from about 12 million hectares in 1984/1985 to about 9 million hectares in 1988/1989. Australian resources previously employed in grain production flowed into the livestock sector and into alternative crops, such as legumes. They acknowledged that the EEP is only one of a number of factors contributing to the decline in Australian wheat export earnings. However, in their opinion the EEP has clearly had a significant adverse impact on Australian agricultural exports.

U.S. Agriculture officials stated that the EEP's effects on wheat prices were minimal to begin with and were mitigated by the Australian government's guaranteed price mechanism and devaluation of the Australian dollar in 1985. They attribute recent declines in Australian wheat production to historically high wool prices during the mid-1980s, which lured farmers out of wheat and into wool production.

Canada

Canadian officials could not demonstrate a loss in market share directly related to EEP; instead they criticized EEP's price depressing effect and the resultant decreased revenue from agricultural exports. They also complained that EEP's targeting strategy was inconsistent and questioned its continued use for commodities which were in short supply. For example, the officials noted that Canada, not the EC, had established major wheat markets in Iraq, Colombia, Mexico, and the Philippines, yet they were all targeted under EEP. In addition, Saudi Arabia was a large importer of barley from many sources, not just the EC. When an EEP initiative for barley was announced, the whole balance of the barley trade was upset.

Canadian officials also questioned EEP wheat sales during the last 2 years when supplies were greatly reduced due to worldwide drought conditions. In their view, the United States was the "only game in town," yet it sold EEP wheat to China and the Soviet Union, the largest importers of wheat in the world. Canadian officials viewed the use of EEP as "overkill" in these cases.

Despite the perceived negative effects of the EEP on export strategies, world price, and the balance of trade, Canada has derived some indirect benefits. In the last year, Canadian

exports of rapeseed oil, or canola, have become very competitive in U.S. markets partly because of high U.S. domestic vegetable oil prices driven up (or artificially supported) by EEP. According to Canadian officials, annual sales of vegetable oil to the United States have increased sixfold. In addition, U.S. livestock growers have been paying higher feed grain prices, driving up the cost of U.S. meat products. As a result, Canadian pork products are more competitive in the U.S. domestic market.

Proposal Tracking Process

FAS processes each EEP targeting proposal through one of three different divisions depending on the commodity. Once these divisions have analyzed a proposal it is sent to FAS management for review, and then to Agriculture's Under Secretary for International Affairs and Commodity Programs. Should the Under Secretary approve the proposal, it is sent through an interagency approval process and, if accepted, announced to exporters.

We found that FAS does not centrally track the progress of these proposals from the moment they are received to the time they are either accepted or rejected. Although documentation exists which discusses reasons for acceptance or rejection, the time that it takes proposals to move within the process cannot always be determined. We believe that FAS should establish a centralized tracking system which will document the progress of

all proposals from the time they are submitted until the time they are accepted or rejected. This system should allow FAS to provide the full history and current status of any proposal when an inquiry is made.

Setting Price And Bonus Levels

The OIG reported that FAS "did not have written policies and procedures for, or sufficient documentation to support, world price determinations and bonus calculations." Our ongoing review indicates that FAS does not sufficiently document the specific figures used to calculate the final price and bonus levels.

FAS gathers information from a variety of sources to use in calculating price and bonus levels. We interviewed a number of individuals who provide EC price and world freight information and we reviewed documents they sent to FAS. We believe that FAS program officials receive the information necessary to make informed and effective price and bonus decisions; however, they do not document adjustments made to this information when calculating price and bonus levels. Although FAS officials prepare price sheets which list each of the figures used in price and bonus calculations, they do not provide either narrative or statistical support to explain how they arrived at these figures. As a result, it is difficult for an independent reviewer to determine whether bonus payments are excessive.

Internal Control Weaknesses

The OIG report identified several internal control weaknesses in the EEP dairy cattle program, including controls over exporter participation requirements and bonus payments. In addition, our review identified internal control weaknesses in the bonus payment process which allowed overpayments to occur.

Exporter qualification requirements

FAS has established certain qualification requirements for exporters wishing to participate in EEP. For example, exporters are required to have sales contracts with importers prior to submitting bids on EEP sales. However, the OIG found that FAS had not been requiring exporters to submit evidence of sales contracts. Beginning in July 1988, FAS has required such proof prior to bidding only on EEP dairy cattle sales.

The OIG report recommends that FAS define minimum requirements for a properly executed sales contract and extend the requirement for proof to all EEP commodities. FAS opposes these actions because they would cause serious delay in the review and award of bonuses and would greatly tax existing staff resources.

We believe that requiring exporters to document the existence of sales contracts prior to submitting bids represents a sound control mechanism. In addition, we believe that FAS should randomly verify that the sales contracts are valid.

Bonus payment procedures

OIG's and our review of EEP demonstrates that FAS has inadequate internal controls over the processing and payment of bonuses to exporters. Specifically, the OIG found that FAS paid bonuses to exporters for shipment of commodities not contained in the applicable sales agreement. We found that FAS lacks the internal controls necessary to ensure that exporters do not get bonuses for shipments in excess of the amount stated in the contract agreement.

During our review, we examined contract files kept by the Agricultural Stabilization and Conservation Service (ASCS) in Kansas City. We also obtained and examined a copy of the data base jointly developed by FAS and ASCS which contains contract and payment information and is maintained by ASCS in Kansas City. We found eight cases where exporters had received overpayments totaling more than $635,000. These overpayments were made because FAS did not have procedures set up to identify and verify when an exporter had received the maximum bonus amount allowed under the contract.

We discussed this problem with the FAS Administrator and suggested that he may want to implement an internally developed proposal which FAS officials believe could virtually eliminate the problem of overpayments. This proposal would change the data base so that it would alert ASCS when a bonus payment ceiling has been reached.

The Future of EEP

There are widely divergent views concerning the need for EEP today. Some view the program positively, while others are critical. On the positive side, the farm community generally sees EEP as largely responsible for the increase in wheat exports over the last several years and views it as a valuable export assistance tool.

The U.S. government views EEP as a valuable trade policy tool which has encouraged the EC to negotiate the liberalization of agricultural trade in the Uruguay Round of the multilateral trade negotiations. It recognizes that the program must be used judiciously, given current market supply conditions, but strongly emphasizes that it must not be unilaterally dismantled. If market conditions were to change, EEP could be used more aggressively, thereby increasing the costs of the EC export subsidy program and applying pressure on them to negotiate. The

U.S. government maintains that eliminating the program now would send the wrong signal to the EC and others concerning the political will of the United States to combat foreign agricultural export subsidies.

Some critics charge that the program has generated little, if any, increase in U.S. agriculture exports. They also question whether subsidies are necessary for wheat sales, given the relatively tight supply conditions. Furthermore, some question whether supplies of U.S. commodities are adequate to support aggressive use of the EEP and whether U.S. domestic prices might not increase if the program is used too aggressively.

Other competitors complain that they have been caught in the cross-fire of the subsidy war between the United States and the EC and that EEP has caused world commodity prices to decrease, thereby affecting their revenues.

While most U.S. observers would agree that EEP was instrumental in bringing the EC to the negotiating table initially, their views differ as to its present utility in encouraging serious negotiations to liberalize agricultural trade. The outcome of the agricultural trade negotiations remains unclear, with the United States and the EC still disagreeing over the ultimate objectives.

EC officials told us that EEP has had little effect in recent months in moderating their position on the agricultural trade negotiations. However, U.S. negotiators, including the U.S. Trade Representative and the Secretary of Agriculture, have reaffirmed the U.S. position that U.S. competitors should not expect any unilateral concessions by the United States. Agriculture's Under Secretary for International Affairs and Commodity Programs stated in May 1989 that there was a continued role for EEP. Regardless of the perceived degree of EEP's usefulness in the current market environment, the U.S. administration has made it clear that it is not going to give up EEP unilaterally.

In today's tighter wheat market, we believe that EEP is appropriately being used more selectively. It remains an important trade policy tool if for no other reason than that unilaterally abandoning it would weaken the U.S. negotiating position with the EC. However, because of large, continuing EC export subsidies, funding EEP at adequate levels is important to maintaining the program's credibility as a trade policy tool. If market conditions change, EEP could again be used aggressively, potentially increasing the cost of the EC's subsidy program and applying pressure to negotiate.

GSM-102/103 EXPORT CREDIT GUARANTEE PROGRAMS

Our current review was requested by the Chairman, Subcommittee on Tobacco and Peanuts, House Committee on Agriculture. The Commodity Credit Corporation's (CCC) GSM-102/103 Export Credit Guarantee Programs are intended to maintain or increase U.S. agricultural commodity exports by guaranteeing exporters or their assignees that they will be repaid for credit sales made to purchasers in foreign countries. Should a foreign buyer default, CCC will make good on the payment and then try to recoup the loss from the foreign buyer.

The two CCC programs are administered by FAS. In June 1988, we issued a report[5] on these programs in which we concluded that FAS was not adequately managing them. More specifically, we stated that CCC had not adequately (1) accounted for outstanding guarantees, (2) ensured that guarantees are used for U.S. agricultural commodities, and (3) provided guidance to program users. We recommended that the Secretary of Agriculture direct the General Sales Manager, FAS, to

-- enforce compliance with the requirement that exporters submit complete reports of exports to ensure accurate accounting of outstanding guarantees;

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[5]Commodity Credit Corporation's Export Credit Guarantee Programs (GAO/NSIAD-88-194).

-- design, develop, test, and implement internal controls, including random on-site verifications, to ensure that loan guarantees are used to obtain U.S. agricultural commodities;

-- clarify program regulations with specific definitions for a U.S. agricultural commodity and a firm sale, and require acknowledgement of these requirements on guarantee applications; and

-- provide timely and accurate decisions on document revisions requested by exporters or their assignees.

We are pleased to report that FAS has taken action on some of our recommendations. However, work conducted since June 1988 by both Agriculture's OIG and GAO indicates that further FAS action is needed to address our original concerns about implementing internal controls and defining an agricultural commodity. Actions are also still needed on our concerns about the timely handling of revisions to GSM documentation. Finally, we have comments to make about the participation of U.S. financial institutions in the GSM programs.

Actions Taken on Previous GAO Recommendations

FAS has acted on our recommendations to improve the accounting of outstanding guarantees and to establish internal controls.

For GSM-102/103 guarantees outstanding, when exporters fail to submit the required export sale loan repayment schedule, ASCS officials, who perform CCC's accounting services, compute their own estimated repayment schedules using the terms identified on available GSM sale documentation and the current London Interbank Offer Rate (LIBOR), plus one quarter of one percent. If the official repayment schedule is later received, ASCS will make adjustments as necessary. According to ASCS officials, only minor adjustments have been required to date.

FAS has established some internal controls over the programs. Effective October 1, 1988, exporters must certify to FAS the foreign origin content of the export sales they register under the GSM-102/103 programs. At this time, they must certify that zero percent value of foreign origin content is included in the export sale. The validity of the certification statements will be spot-checked by the FAS Compliance Review Office, which has been given additional resources for reviewing compliance with this and other GSM-102/103 regulations.

We believe that the actions taken by FAS are important steps in improving management of the GSM-102/103 programs. However, much more is needed before firm control over program operations is achieved.

Further Improvements Needed in Internal Controls

Recent work conducted by the OIG and GAO has shown that further internal controls over the GSM-102/103 programs are necessary. A September 29, 1989, OIG report[6] stated that compliance review efforts are needed and that suspension and debarment actions should be used whenever exporters are found to violate program regulations. Our review also indicates that controls are not in place to ensure that exporters are complying with applicable regulations.

Additional compliance review efforts are needed

The OIG report stated that "U.S. exporters are participating in a $6 billion program without FAS or CCC conducting a review, or periodic check, to make sure the program is operating in accordance with applicable laws and regulations." Some compliance review efforts have now been undertaken. However, our

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[6]Audit of the Foreign Agricultural Service Exports of the Foreign Commodities Under GSM 102/103, Audit Report No. 07099-21-Hy.

review work indicates that more compliance review efforts are necessary.

Our June 1988 report recommendation on internal controls called for random, on-site verifications of export commodities in order to ascertain that U.S. agricultural commodities are being financed by the guarantee programs. We believe this is an important control because CCC and FAS officials deal only with the paperwork aspects of the guarantee programs. Without physically inspecting the commodities being exported at both U.S. export terminals and foreign import terminals, at least on a spot-check basis, CCC and FAS officials cannot be certain that only U.S. agricultural commodities are being financed under the program. The OIG identified some foreign origin commodities that were financed and our work within the past year further reinforces the need for on-site verifications.

With assistance from U.S. Customs, we made random inspections at U.S. ports holding seven tobacco export shipments destined for countries under the GSM programs. In one instance, Customs officials believe that over 80 percent of the tobacco in that sale was of foreign origin. In another instance, we visited an exporter who was participating in the GSM-102 program for grocery items and found that he was preparing for shipment several items that contained foreign origin content, including coffee filters manufactured in Canada.

As a further assurance that U.S. agricultural commodities financed under the GSM-102/103 programs are being delivered to the intended destinations, FAS should conduct periodic spot inspections at foreign ports. This can easily be accomplished by FAS staff assigned overseas or by FAS officials, e.g., compliance review staff, in travel status. In the past, FAS officials have stated that time and resources were not available for this type of monitoring and oversight.

According to foreign officials, random checks at foreign ports are possible. While conducting work at four overseas locations this past summer, we asked foreign government officials if it would be possible for FAS officials to inspect the off-loading of GSM commodities at their ports of entry to ensure that the commodities were U.S. agricultural products. In all but one instance, we were told that FAS access to the ports for inspection would be allowed. In that one instance, we were advised that obtaining permission for access would be difficult because the port is used for closely guarded military operations as well as civilian operations.

CCC should take suspension or debarment actions where appropriate

The OIG report stated that FAS should use established compliance measures, such as suspension or debarment, to discourage U.S. exporters from blending or combining foreign

origin agricultural commodities or products with U.S. commodities for export under the GSM programs.

Considerable attention has been focused on the suspension and debarment issue, because a number of tobacco exporters who have shipped large quantities of foreign tobacco as U.S. tobacco under the export credit guarantee programs continue to participate in the programs. In prior testimony we noted that FAS does not intend to initiate suspension or debarment proceedings while the U.S. Attorney's investigation continues, so as not to impair his case. However, in May of this year, the Director of CCC's Operations Division wrote letters to 31 exporting companies, representing 92 different GSM guarantees, stating that as a result of the OIG audit, it had been determined that the exporters may have violated GSM program requirements by exporting non-U.S. commodities. The letters put the exporters on notice that they may be held liable to CCC for any amounts paid or that may be paid by CCC under the guarantees.

When significant violations occur, we believe that suspension or debarment proceedings would be the appropriate agency response and that Agriculture should be prepared to initiate such actions. According to FAS officials, they will take appropriate actions in the future when evidence is developed that shows that violations have occurred. New compliance review

efforts could assist in identifying program violators and documenting the evidence of wrongdoing.

An Eligible Agricultural Commodity Still Needs to be Defined

The OIG report echoes our June 1988 recommendation concerning the need for defining eligible agricultural commodities, especially value added products.

Until September 21, 1988, FAS general policy was to provide export credit guarantee coverage under the GSM-102/103 programs for only those commodities or products containing 100 percent U.S. origin content. While this policy was in effect, credit guarantees were provided for exports of tobacco that were subsequently revealed to contain substantial amounts of foreign tobacco. Also other products, such as grocery items, leather hides and skins, and soft drink concentrates containing some degree of foreign origin content were provided with guarantee coverage under the programs.

On September 21, 1988, FAS announced a new policy that provided credit guarantees for the export of agriculture products that were a mixture of U.S. and foreign origin. The new policy allowed the value of exports under the programs to include up to 25 percent imported agricultural commodities. However, only the value of the U.S. portion of the agricultural commodities would receive the CCC guarantee. This proved to be a highly

contentious policy change. Forty members of Congress questioned this new policy and wrote to the Secretary of Agriculture on October 12, 1988, asking that it be reversed.

On February 15, 1989, FAS discontinued the new policy and notified exporters that beginning February 16, only commodities certified by the exporters to contain zero percent foreign content value would be eligible for program coverage. This policy is still in effect; however, when the February change was made, FAS also announced that it would reevaluate the content issue. In a related matter, Agriculture's General Counsel stated in May 1989 that exports under the programs would be eligible even if they contained small amounts of non-agricultural products.

Based on our work thus far, we believe that the current zero percent foreign value content policy may be appropriate for exports of bulk commodities such as wheat, corn, barley, and tobacco. However, that policy may be inappropriate for processed agricultural products, many of which may contain small amounts of foreign origin ingredients. For example, powdered infant formula containing foreign origin ingredients that account for only 2 percent of the total value of the product is excluded from coverage under the current policy, as is soft drink concentrate with a small percentage of foreign content. A comprehensive

evaluation of the foreign content issue should include an assessment of how to handle such products.

FAS is continuing to evaluate the foreign content issue. As we stated in the past, the history of the foreign content issue and the fact that the last two program policy announcements were made by FAS without comprehensive evaluations makes it all the more important that FAS conduct its current assessment of the foreign content question in a comprehensive and systematic manner. A positive aspect of the evaluation is that on May 22, 1989, FAS published a Federal Register notice soliciting public comment on the foreign content issue. Of the 18 comments received, 13 disagreed with the current policy of zero percent foreign content. At least 7 of these comments represented the agricultural seed industry. The others represented exporters of leaf tobacco and value added products. Four comments agreed with the current policy; they represented the bulk grain industry. Comments filed by one organization did not clearly state a position. We believe FAS efforts to obtain participant views are a step in the right direction. However, more needs to be done.

One way to help achieve a comprehensive evaluation of the policy issues is to establish a working group of representatives of interested parties to review and debate the issues and to develop options for FAS consideration. FAS has established an internal working group to deal with the issue. We feel this

effort should be expanded to include participation by other interested parties.

Action Still Needed on the Timely Handling of Revisions to GSM Documentation

Our June 1988 report suggested that CCC be more flexible with exporters and financial institutions when changes to GSM documentation were necessary. We cited an example of a U.S. bank that spent 8 months trying to get CCC to correct the name of a foreign bank placed on the guarantee document by CCC officials. This change was very important to the U.S. bank because a CCC official stated that guarantees may become invalid if documentation is not properly prepared. CCC, rather than making the correction itself, wanted the U.S. bank to obtain written assurance from the foreign bank that it would honor the incorrectly named bank on the document. Eventually, CCC did make the correction, but the U.S. bank officials claimed they spent too much time and effort on an error that was made by CCC.

During recent discussions with several exporters and U.S. financial institutions participating in the GSM programs, we were told of several other similar instances that frustrated exporter and bank officials. In one case, documentation prepared by the U.S. bank regarding a repayment due in three equal installments was not accepted by CCC because of the way the bank rounded the cents on a whole dollar. Apparently the bank showed that 34

cents would be collected as part of the first installment and 33 cents as part of the second and third installments. CCC returned the documentation and requested that 33 cents be shown as part of the first and second installments and 34 cents on the third.

Participation of Financial Institutions in the GSM Programs

The success of the GSM-102/103 programs depends greatly on the active participation of financial institutions, which pay out the $4 billion to $6 billion in GSM loans each year, providing direct credit to the foreign buyers. According to CCC records, two financial institutions--The National Bank for Cooperatives and the Banca Nazionale del Lavoro--have been significant program participants. Together, they have provided approximately one-third of the money loaned under GSM-102 during the past 5 years and approximately three-fourths of the money loaned under GSM-103 during the past 3 years. The remainder of the program loans have been provided by numerous other financial institutions, each loaning lesser amounts of money.

From discussions with officials of several of these financial institutions, it appears that the government guaranteed loan business is not particularly profitable and is therefore attractive only to (1) U.S. financial institutions specializing in government loans or (2) foreign-owned banks trying to get established in the United States.

The National Bank for Cooperatives

The National Bank for Cooperatives specializes in government loans. Officials there said that over 90 percent of their business involves loans with CCC, the Export-Import Bank, or some other government agency loan program. The Bank was established through federal legislation in 1933 to finance sales by U.S. cooperative farmer organizations. Today it is wholly owned by its cooperative members. The Bank is a member of the Farm Credit System, which has U.S. government agency status. Privileges derived from its agency status allow the Farm Credit System to raise or obtain funds at a lower cost than commercial banks. Therefore, as a member of the Farm Credit System, the National Bank for Cooperatives obtains funds at a lower cost and obtains a higher profit margin in the government loan business than would commercial banks.

Bank officials told us that, in spite of operational problems, they believe the GSM programs are two of the best programs ever established to facilitate the export of U.S. goods. They said that the Bank plans to continue its participation in the programs.

Banca Nazionale del Lavoro

The Banca Nazionale del Lavoro is Italy's largest state-owned bank. It is headquartered in Rome but has several branches in the United States. The New York City branch is responsible for North American operations, but the Atlanta, Georgia, branch provides the GSM loans. Officials of the Bank's Atlanta branch told us that the majority of their business involves GSM loans to Iraq. Iraq imports about $1.0 billion worth of U.S. agricultural commodities under the GSM-102/103 programs each year.

Recently, the Bank has been embroiled in controversy. According to Bank officials, its Atlanta branch loaned about $2.0 billion to foreign buyers in Iraq. Only a fraction of that amount was authorized by higher level Bank officials. They told us that some of these loans, amounting to about $830 million, were made under the GSM-102/103 programs and of that amount, only about $130 million was authorized. They said other loans to Iraq were made outside government programs. The unauthorized loans and the adequacy of the Bank's internal controls are currently being investigated by several U.S. and Italian agencies. The status of the investigation has not been made public.

Bank officials are concerned about having such a large exposure in one country; they told us that although Iraq has been making regular payments and has never defaulted, it is classified

by many banks as a high credit risk due to its war with Iran and the resulting depletion of its foreign exchange reserves.

We were recently told by Banca Nazionale del Lavoro's New York branch officials that officials in Rome will have to decide whether or not the Bank will continue to participate in the program, including making new GSM loans to Iraq. If the Bank decides not to make any new GSM loans, then FAS will lose a major participating financial institution whose business will have to be made up by other banks if CCC's guarantee targets are to be achieved.

The Banca Nazionale del Lavoro's problems may or may not result in CCC payouts under its loan guarantee programs, but they raise a question concerning the wisdom of allowing one bank to participate to such a large extent in the programs, especially if the bank's loan exposure is going to be concentrated in a single country. In light of these problems, FAS may want to examine the issue of bank participation in the programs.

Messrs. Chairmen and Members of the Subcommittees, this completes my statement. I will be happy to answer any questions you may have.

(Attachments follow:)

ATTACHMENT I

ATTACHMENT I

TARGETED EXPORT ASSISTANCE PROGRAM PARTICIPANTS, FY 1986 - 1990

NON-PROFIT APPLICANT ORGANIZATIONS	ALLOCATED AMOUNT IN ($) FY 1986	FY 1987	FY 1988	FY 1989	FY 1990
1 Alaska Seafood Marketing Institute		1,500,000	1,950,000	6,000,000	4,500,000
2 American Plywood Association	1,950,000	1,980,000	1,200,000	7,700,000	6,500,000
3 American Seed Trade Association		350,000			
4 American Sheep Producers Council, Inc.				100,000	148,000
5 American Soybean Association	8,500,000		9,800,000	11,450,000	11,500,000
6 California Avocado Commission		420,000	450,000	650,000	
7 California Cling Peach Advisory Board	1,500,000	5,600,000	5,700,000	4,700,000	3,500,000
8 California Kiwifruit Commission		500,000	500,000	1,000,000	900,000
9 California Pistachio Commission	200,000	200,000		500,000	750,000
10 California Prune Board	4,000,000	4,500,000	5,500,000	5,000,000	7,500,000
11 California Raisin Advisory Board	6,300,000	9,000,000	9,000,000	10,700,000	12,500,000
12 California Strawberry Advisory Board					500,000
13 California Table Grape Commission	350,000	450,000	750,000	1,850,000	2,300,000
14 California Tree Fruit Agreement					500,000
15 California Walnut Commission	9,000,000	7,000,000	6,500,000	7,300,000	8,000,000
16 Catfish Farmers of America			50,000	150,000	
17 Cherry Marketing Institute, Inc.				500,000	400,000
18 Chocolate Manufacturers Association of America	2,500,000		2,500,000	3,000,000	900,000
19 Concord Grape Association				1,500,000	700,000
20 Cotton Council International	7,000,000	6,800,000	1,450,000	15,000,000	15,400,000
21 Eastern United States Agricultural and Food Export Council, Inc. (EUSAFEC)	1,100,000	1,000,000	1,100,000	2,100,000	2,950,000
22 Export Incentive Program (Almonds)	900,000	4,180,000	6,500,000	11,800,000	9,000,000
23 Export Incentive Program (Citrus)	8,500,000	10,500,000	10,500,000	11,200,000	8,800,000
24 Export Incentive Program (Mink)		1,500,000	700,000		
25 Export Incentive Program (Processed Corn)			1,500,000	1,250,000	1,250,000
26 Florida Department of Citrus	4,600,000	7,000,000	7,000,000	5,400,000	5,900,000
27 Hop Growers of America					50,000
28 Kentucky Distillers' Association					2,000,000
29 Leather Industries of America		1,500,000	1,500,000	1,800,000	
30 Mid-America International Agricultural Trade Council (MIATCO)	800,000	1,200,000	1,100,000	1,900,000	2,700,000
31 National Association of Animal Breeders				400,000	402,000
32 National Association of State Departments of Agriculture (NASDA)	500,000			100,000	750,000
33 National Council of Farmer Cooperatives			350,000	300,000	
34 National Dry Bean Council			800,000	1,000,000	
35 National Forest Products Association				6,150,000	7,400,000
36 National Hay Association		300,000			
37 National Honey Board				500,000	1,000,000
38 National Pasta Association	2,100,000				
39 National Peanut Council	4,500,000	4,500,000	1,500,000	7,400,000	4,500,000
40 National Potato Promotion Board	2,000,000	2,550,000	2,400,000	4,700,000	4,800,000
41 National Sunflower Association		3,000,000		2,400,000	4,000,000
42 Northwest Horticural Council Northwest Cherry Growers		120,000	450,000	800,000	1,000,000
43 Northwest Horticural Council Oregon-Washington-California Pear Bureau	300,000	400,000	500,000	800,000	900,000
44 Northwest Horticural Council Washington State Apple Commission	1,400,000	1,500,000	2,000,000	3,850,000	3,800,000

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TARGETED EXPORT ASSISTANCE PROGRAM PARTICIPANTS, FY 1986 - 1990

NON-PROFIT APPLICANT ORGANIZATIONS	ALLOCATED AMOUNT IN ($) FY 1986	FY 1987	FY 1988	FY 1989	FY 1990
45 Rice Council for Market Development	3,500,000	3,500,000	4,500,000	5,700,000	8,500,000
46 Southern United States Trade Association (SUSTA)	800,000	800,000	1,100,000	1,900,000	2,700,000
47 Texas Produce Export Association					150,000
48 Tobacco Associates, Inc.		900,000	400,000	2,750,000	5,000,000
49 USA Dry Pea and Lentil Council	2,500,000	2,500,000	3,000,000	1,000,000	
50 USA Poultry and Egg Export Council	6,000,000	6,500,000	4,250,000	8,000,000	6,000,000
51 U.S. Feed Grains Council	11,100,000	2,800,000	2,400,000	4,200,000	6,000,000
52 U.S. Meat Export Federation	7,000,000	7,000,000	4,500,000	17,300,000	9,000,000
53 U.S. Hide Export Development Council				2,500,000	1,500,000
54 U.S. Wheat Associates, Inc.	3,100,000	3,100,000	1,200,000	4,900,000	5,200,000
55 Western United States Agricultural Trade Association (WUSATA)	2,200,000	1,950,000	1,600,000	4,300,000	5,250,000
56 Wine Institute	4,800,000	2,600,000	3,000,000	7,000,000	9,000,000
TOTAL:	110,000,000	110,000,000	110,000,000	200,000,000	200,000,000

TARGETED EXPORT ASSISTANCE PROGRAM
TOP FIFTEEN ALLOCATION REPORT

NON-PROFIT APPLICANT ORGANIZATIONS	COMMODITY	ALLOCATED AMOUNT IN ($) FY 1986	% of FUNDS\1	FY 1987	% of FUNDS	FY 1988	% of FUNDS	FY 1989	% of FUNDS	FY 1990	% of FUNDS	TOTAL FUNDING FY86 - FY90	% OF TOTAL FUNDING
1 Export Incentive Program (Citrus)	Citrus	8,500,000	7.73	10,500,000	9.55	10,500,000	9.55	11,200,000	5.60	8,899,000	4.40	49,500,032	6.78
2 California Raisin Advisory Board	Raisins	6,300,000	5.73	9,000,000	8.91	9,000,000	8.91	10,700,000	5.35	12,500,000	6.25	48,100,029	6.73
3 Cotton Council International	Cotton	7,000,000	6.36	6,000,000	6.18	1,450,000	1.32	15,000,000	7.50	15,460,000	7.70	45,050,021	6.25
4 U.S. Meat Export Federation	Meat	7,000,000	6.36	7,000,000	6.36	4,500,000	4.09	17,000,000	8.50	9,000,000	4.50	44,500,025	6.10
5 American Soybean Association	Soybeans	8,500,000	7.73			9,000,000	8.91	11,450,000	5.73	11,500,000	5.75	41,250,022	5.65
6 California Walnut Commission	Walnuts	9,000,000	8.18	7,000,000	6.36	6,500,000	5.91	7,300,000	3.65	8,000,000	4.00	37,000,024	5.10
7 Florida Department of Citrus	Citrus	4,000,000	4.18	7,000,000	6.36	7,000,000	6.36	5,400,000	2.70	9,000,000	4.05	33,900,020	4.64
8 Export Incentive Program (Almonds)	Almonds	900,000	0.82	4,100,000	3.00	6,500,000	5.91	11,000,000	5.50	9,000,000	4.50	32,300,016	4.44
9 USA Poultry and Egg Export Council	Poultry & Eggs	6,000,000	5.45	6,500,000	5.91	4,250,000	3.86	8,000,000	4.00	6,000,000	3.00	30,750,019	4.21
10 California Prune Board	Prunes	4,000,000	3.64	4,500,000	4.09	5,500,000	5.00	5,000,000	2.50	7,500,000	3.75	27,300,016	3.74
11 U.S. Feed Grains Council	Feed Grains	11,100,000	10.09	2,800,000	2.55	2,400,000	2.18	4,200,000	2.10	6,000,000	3.00	26,500,017	3.63
12 Rice Council for Market Development	Rice	3,500,000	3.18	3,500,000	3.18	4,500,000	4.09	5,700,000	2.85	8,500,000	4.25	25,700,013	3.52
13 National Peanut Council	Peanuts	4,500,000	4.09	4,500,000	4.09	1,500,000	1.36	7,400,000	3.70	4,500,000	2.25	22,400,013	3.07
14 California Cling Peach Advisory Board	Peaches	2,500,000	2.27	5,600,000	5.09	5,700,000	5.18	4,700,000	2.35	3,500,000	1.75	22,000,015	3.01
15 American Plywood Association	Plywood	1,950,000	1.77	1,900,000	1.00	1,200,000	1.09	7,700,000	3.85	6,500,000	3.25	19,330,009	2.65
			77.59		74.24		73.73		66.68		63.30		69.60

\1 Percentage of TEA funds allocated are based on an allocation level of $110 million for fiscal years 1986 thru 1988, and $200 million for fiscal years 1989 and 1990.

ATTACHMENT 11

ATTACHMENT III

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TARGETED EXPORT ASSISTANCE PROGRAM
BUDGET REPORT BY COUNTRY
BASED ON TEA ACTIVITY PLANS
FISCAL YEAR 1989

(THE TOP 16 COUNTRIES OUT OF A TOTAL OF 53 RECEIVING MORE THAN $1 MILLION)

COUNTRY	REGION	TOTAL FY89 BUDGET	% OF FY89 TEA FUNDS BUDGETED ($126,936,795)\1
JAPAN	ASIA	46,054,336	36.28
UNITED KINGDOM	EC	15,323,894	12.07
FEDERAL REPUBLIC OF WEST GERMANY	EC	10,752,555	8.47
AUSTRALIA	OCEANIA	9,353,132	7.37
CHINA	ASIA	6,792,813	5.35
REPUBLIC OF KOREA	ASIA	5,475,168	4.31
HONG KONG	ASIA	3,951,733	3.11
FRANCE	EC	3,892,645	3.07
ALGERIA	NORTH AFRICA	3,238,350	2.55
ITALY	EC	2,428,791	1.91
SPAIN	EC	2,312,265	1.82
EGYPT	NORTH AFRICA	2,246,840	1.77
MOROCCO	NORTH AFRICA	1,540,024	1.21
NETHERLANDS	EC	1,406,655	1.11
PORTUGAL	EC	1,191,350	0.94
SINGAPORE	ASIA	1,026,917	0.81
	TOTAL:	$116,987,468	92.16

\1 The budgeted amount of $126,936,795 reflects the most recent FAS Budget by Country report dated 10/4/1989. FAS officials have not yet updated this report, but have confirmed that the amount of $126,936,795 represents approximately 70% of the total FY 1989 budgeted TEA funds.